Rheinmetall AG
Annual Report 2003

RHEINMETALL

Rheinmetall in figures

	Rheinmetall Group in figures		1999	2000	2001	2002	2003
			HGB				
	Net sales	€ million	4,514	4,570	4,603	4,571	**4,248**
	Order intake	€ million	4,740	4,563	5,033	4,840	**4,128**
	Order backlog (Dec. 31)	€ million	4,147	3,732	4,113	4,165	**3,143**
	EBITDA	€ million	296	374	468	701	**446**
	EBIT	€ million	66	103	195	392	**204**
	EBT	€ million	30	2	84	290	**120**
	Net income/(loss)	€ million	(6)	(43)	38	274	**68**
	Cash flow	€ million	254	239	315	587	**308**
	Capital expenditures	€ million	293	265	284	248	**203**
1	Amortization/depreciation/write-down	€ million	224	251	247	268	**211**
	Accounting equity	€ million	553	691	717	869	**731**
	Total assets	€ million	3,474	4,477	4,218	4,087	**3,442**
	EBIT margin	in %	1.5	2.3	4.2	8.6	**4.8**
	ROCE	in %	6.2	4.3	8.8	20.1	**12.3**
	Earnings per share (EpS) (DVFA/SG)	€	(0.25)	--	--	--	**--**
	Earnings per common share (IAS)	€	--	(1.33)	0.56	6.81	**1.72**
	Earnings per preferred share (IAS)	€	--	(1.27)	0.62	6.87	**1.78**
	Total dividend distributed	€ million	17	24	17	24	**24**
2	Dividend per common share	€	0.44	0.64	0.44	0.64	**0.64**
2	Dividend per preferred share	€	0.50	0.70	0.50	0.70	**0.70**
	Employees (Dec. 31)		33,050	29,876	27,828	25,949	**20,888**

1 *Excl. goodwill amortization*

2 *Incl. bonus of €0.20 in 2000 and 2002*

Cover

Historical home with latter-day enlargement: Rheinmetall AG's corporate headquarters in Düsseldorf's Derendorf district

The Rheinmetall Group at a glance

Rheinmetall AG

Management holding company

Rheinmetall is a group squarely focused on its two corporate sectors: Automotive and Defence.

Run according to principles of local empowerment, Rheinmetall's success rests on the operational impact and vast flexibility of altogether nine divisions subsumed under Kolbenschmidt Pierburg AG and Rheinmetall DeTec AG.

As of December 31, 2003, the management holding company, Rheinmetall AG, held directly or indirectly 95.5 and 100 percent of the stock of Kolbenschmidt Pierburg AG (the rest free-floating) and Rheinmetall DeTec AG, respectively.

Corporate sector Automotive Kolbenschmidt Pierburg AG

Pierburg

Systems and components
for air supply
and emission control

Oil und water pumps,
vacuum pumps

Sales
€880 million

Employees
3,540

Locations
Germany
France
Italy
Spain
USA
Brazil
China (joint venture)

KS Kolben

Passenger car pistons
Piston modules

Commercial-vehicle pistons

Large-bore pistons

Sales
€590 million

Employees
5,480

Locations
Germany
France
Czech Republic
USA
Canada
Brazil
Japan
China (joint venture)

KS Gleitlager

Plain bearings, bushings
Thrust washers

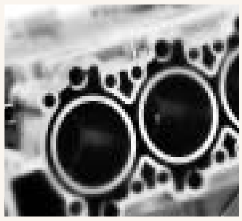
Dry bearings (Permaglide)

Continuous NF castings

Sales
€150 million

Employees
1,000

Locations
Germany
USA
Brazil



KS Aluminium-Technologie

Engine blocks

Sales
€160 million

Employees
910

Locations
Germany

MSI Motor Service International

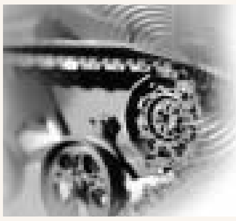
Automotive parts for engine repair and workshops

Sales
€140 million

Employees
340

Locations
Germany
France
Great Britain
Turkey
Brazil

Corporate sector Defence Rheinmetall DeTec AG



Rheinmetall Landsysteme

Armored wheeled and tracked vehicles

Support and mine-clearing systems

NBC protection systems

Turret systems

Sales
€330 million

Employees
1,340

Locations
Germany

Oerlikon Contraves

Air defence systems

Ahead antimissile capability

High-performance radar systems

Simulation and training systems

Sales
€330 million

Employees
1,760

Locations
Germany
Switzerland
Italy
Canada
Singapore
Malaysia

Rheinmetall Waffe und Munition

Weapons and ammunition for tank and artillery systems

Medium-caliber weapons and ammunition

Nonlethal agents

Self-defence systems

Sales
€570 million

Employees
2,870

Locations
Germany
Switzerland

Rheinmetall Defence Electronics

Command, control and reconnaissance systems

C^3I systems

Fire control units

Simulation systems

Sales
€410 million

Employees
1,410

Locations
Germany
Greece

Rheinmetall continuing on track

In fiscal 2003, Rheinmetall again improved its performance while also completing the Group's rebuilding program, successfully evolving from a diversified conglomerate into a neatly structured and transparent Automotive and Defence Group.

The fiscal 2003 figures reflect these efforts:

- ☐ Organic growth of 4+ percent
- ☐ Like-for-like results of operations up by over 20 percent
- ☐ Net financial debts slashed from €301 million to €230 million
- ☐ ROCE at a high 12.3 percent
- ☐ Free cash flow from operations up to €98 million
- ☐ Stock price surges 115 percent

The seeds are sown for added shareholder value enhancement.
This is again the goal and foremost task for 2004.

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News flashes 2003

January

Kolbenschmidt Pierburg
The Electric Fuel Pumps unit is transferred to TI Automotive in Warren, Michigan, as of January 1, 2003

Rheinmetall DeTec
Representatives from STN Atlas Elektronik officially hand over the Magdeburg-based Land Forces Battle Training Center to the Federal Office for Defence Technology and Procurement

Jagenberg
Countdown starts for stockholders to accept Rheinmetall Maschinenbau's public offering

Rheinmetall DeTec
Since the start of the year, Rheinmetall has held a 100-percent stake in Oerlikon Contraves AG

Kolbenschmidt Pierburg
Pierburg's Hartha plant starts up series production of electric coolant pumps that displace conventional V- or tooth-belt drives

Rheinmetall DeTec
Together, Rheinmetall W&M, HDW and KMW demonstrate on the foredeck of the frigate Hamburg, their MONARC, a program for possibly enhancing naval vessel combat impact

February


Copyright: Airbus Industrie

Rheinmetall DeTec
STN Atlas Elektronik wins a megacontract for supplying the electronic controls on the freight loading system for the Airbus A380

Rheinmetall
A new groupwide Young Manager Program grooms would-be and newly appointed managers through coordinated advancement programs designed to facilitate the taking-on of executive positions.

Kolbenschmidt Pierburg
In acquiring Microtechno from Mazda Motor Corporation, KS Kolbenschmidt steps up its activities in Asia

Aditron
Together with partners Berneck-er + Rainer Industrie-Elektronik GmbH, Lenze AG, and Kuka Roboter GmbH, Hirschmann Electronics intends to develop an Ethernet real-time standard

Rheinmetall DeTec
Rheinmetall Landsysteme backs a combination of courses comprising on-the-job training, classroom education, and university studies in the subjects of mechanical and electrical engineering

March

Rheinmetall
Even after the re-indexing of Germany's stock market, Rheinmetall stays a member of the MDAX

Aditron
Rheinmetall says it will squeeze out by cash compensation all minority stockholders

Rheinmetall
attends the Investor Conference staged by Deutsche Bank

Kolbenschmidt Pierburg
accepted for membership in the SDAX market index

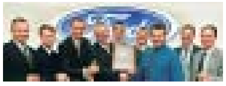
Rheinmetall DeTec
Rheinmetall Landsysteme showcases at the IDEX in Abu Dhabi its new Light Infantry Vehicle for Special Operations

Aditron
At Hannover's CeBIT, Preh-Werke premieres its new modular POS keyboard family

Rheinmetall DeTec
Rheinmetall W&M and Diehl Munitionssysteme sign an agreement on close cooperation in the field of military and civilian high-power microwave technology

Kolbenschmidt Pierburg
During an information gathering tour of North Rhine-Westphalia, the President of the Basque government, J. J. Ibarretxe, calls on Rheinmetall. Ever since 1976, Basque region-based Carbureibar has been an important Pierburg location

April



Kolbenschmidt Pierburg
Ford's Q1 award for supplier excellence goes to the Czech subsidiary Metal Ústí

Rheinmetall
At the annual accounts conference staged in Düsseldorf and with the restructuring drive finalized in all key respects, the Executive Board reports on an excellent performance for fiscal 2002

Kolbenschmidt Pierburg
Rheinmetall announces it will submit a voluntary public offering to the stockholders

Kolbenschmidt Pierburg
Pierburg Hartha hosts a forum for local auto industry vendors attended by Minister President Milbradt

Aditron
Baden-Württemberg's Minister President Erwin Teufel takes a look at Hirschmann Electronics Hannover Fair exhibits for industrial data communication

Kolbenschmidt Pierburg
KS Kolbenschmidt allows students at the European Business School, Oestrich-Winkel, practical insight into key HR management functions

May

Rheinmetall
450 stockholders attend the annual stockholders' meeting in Berlin

Kolbenschmidt Pierburg
attends the Vienna Engine Symposiunm

Rheinmetall DeTec
25 years of weapon building for the Leopard 2

Rheinmetall DeTec
Employees of Rheinmetall Landsysteme go to Kabul to assist paratroopers in the testing of the German armed forces' new vehicle for specialty missions (Wolf ESK)

Rheinmetall DeTec
Rheinmetall Landsysteme hands over to the German army's medical corps the first armored tracked Wiesel 2 and BV206S vehicles

Aditron
The annual stockholders' meeting gives the go-ahead for the squeeze-out proposed by majority stockholder Rheinmetall

June

Aditron
Upon payment of cash compensation to the former stockholders, the outstanding shares are transferred to Rheinmetall

Kolbenschmidt Pierburg
Following the press conference prior to the start of the IAA, journalists take the opportunity to test drive for terrainability a number of SUVs on the site of the European Land Forces Competence Center at Unterlüss

Rheinmetall DeTec
Defence industry journalists from nine European nations attend a meeting at the Competence Center of Weapon & Ammunition showcasing this division's product range

Aditron
Hirschmann Electronics disposes of Hirschmann Austria GmbH, Rankweil

Rheinmetall DeTec
The Koblenz-based Federal Office for Defence Technology and Procurement commissions Rheinmetall Landsysteme and its French associates Thales and MBDA-France with the development of a demonstrable vehicle-supported mine seeking and clearance system

Rheinmetall
Rheinmetall ranks 337th among the FAZ's 500 biggest European companies

Kolbenschmidt Pierburg
With its innovative motor-controlled valve, Pierburg optimizes exhaust gas recirculation

Juli

Aditron
Some 200 participants from industry, science, and the trade media attend the first Industrial Ethernet Congress staged by Hirschmann Electronics in Stuttgart to provide information about the latest trends and developments in automation and network technology

Jagenberg
Rheinmetall Maschinenbau sells its majority stake of 93.7 percent to Kleinewefers-Verwaltungs GmbH

Aditron
Robert Bosch GmbH presents Preh-Werke with its Supplier Award

Kolbenschmidt Pierburg
End of the period for accepting Rheinmetall's voluntary public offering to the remaining stockholders

Rheinmetall DeTec
The French Groupe SAGEM and STN Atlas Elektronik sign an agreement to work together on drones

Rheinmetall
Rheinmetall ranks 44th in size among German industrial companies, says the FAZ newspaper

August

Rheinmetall DeTec
Bremen-based STN Atlas Elektronik GmbH, a subsidiary shared between Rheinmetall DeTec AG and BAE Systems Deutschland GmbH, is split (retroactively as of January 1, 2003) into two separate companies, viz. for land forces and naval technology. The former to operate as Rheinmetall Defence Electronics

Kolbenschmidt Pierburg
Harley Davidson is 100 years old. Numerous of its products use pistons made by the US subsidiary Karl Schmidt Unisia Inc., Marinette

Rheinmetall DeTec
Rheinmetall Landsysteme hands over for a two-month probationary period under the command of the Swiss army a prototype of its new trailblazing sapper tank, an offshoot of the Leopard 2 battle tank

Kolbenschmidt Pierburg
The Hannover-based Internationale Gesellschaft für Kunststofftechnik e.V. presents Pierburg its SPE Automotive Division Award 2003 for Pierburg's VW intake manifold module and for the BMW V8 intake manifold module

Aditron
Together with its associate Pérez Cloquel, Hirschmann Electronics installs a communication network for over 1,200 terminals at Europe's tallest (186 meters) holiday resort, the Gran Hotel Bali, Benidorm

September

Rheinmetall DeTec
Nitrochemie Aschau celebrates its 50th anniversary

Kolbenschmidt Pierburg
Pierburg's newly developed fully variable vane-type oil pump makes its debut at the 60th IAA, Frankfurt

Aditron
Hirschmann Electronics and Preh-Werke for the first time have a joint stand at the world's biggest auto show; a glass model shows the arrangement of all these companies' key systems and components

Rheinmetall DeTec
Germany's Defence Minister Struck calls on Rheinmetall's Unterlüss location

Rheinmetall DeTec
Rheinmetall Defence Electronics starts up the new production plant at Rostock, a supplier to the Airbus builders

Rheinmetall DeTec
At London's DSEi, Rheinmetall Landsysteme showcases its reconnaissance and combat vehicle

Rheinmetall DeTec
Rheinmetall Landsysteme's Family Day in Kassel proves a great success

Rheinmetall DeTec
Oerlikon Contraves Pyrotec celebrates the 50th anniversary of the Ochsenboden Testing Center which also tries out defence systems

October

Aditron
In its efforts to concentrate on the core businesses of Automotive and Defence, Rheinmetall sells its stake in Preh-Werke to Deutsche Beteiligungs AG

Rheinmetall
Düsseldorf opens up its archives to members of the public interested in researching the city's history. Rheinmetall organizes an exhibition on the subject of Automotive Engineering

Rheinmetall DeTec
Rheinmetall Landsysteme supplies to the US Army base at Fort Belvoir, Washington, the prototype of Hailstorm for defusing mines and detecting duds at a safe distance

Kolbenschmidt Pierburg
MSI Motor Service International GmbH and KS Motorac exhibit jointly at Equip' Auto 2003 in Paris, after automechanika, the world's biggest aftermarket show

Aditron
The merger of the parent company of the Electronics sector into Rheinmetall AG takes effect

EMG EuroMarine Electronics
EquiVest takes over from EMG EuroMarine Electronics, a Rheinmetall subsidiary, the STN Atlas Marine Electronics business

Kolbenschmidt Pierburg
displays its latest engineering innovations as part of a concerted effort under the auspices of the German Auto Industry Association at the Tokyo Motorshow

November

Rheinmetall
Members of the sectors' HR and other departments represent the Group for the fourth time in succession at the German Graduates Congress

Rheinmetall
Market capitalization breaks the €1 billion barrier

Kolbenschmidt Pierburg
Rheinmetall lifts its stake to 95.5 percent

Kolbenschmidt Pierburg
Now that the free float has sunk below 5 percent, the shares are listed in the Prime Standard

Rheinmetall
Shares hit annual highs (floor of the Frankfurt/Main exchange).

Common:	€28,90
Preferred:	€28,86

Rheinmetall DeTec
For the third time running, an apprentice at Rheinmetall W&M is awarded top-of-the-state grades in his trade by the Lower Saxony Chamber of Commerce & Industry

Rheinmetall
attends the Berenberg Bank's Investor Conference

Rheinmetall DeTec
The Rheinmetall DeTec Group companies are awarded a megacontract as a result of an order from NATO partner Greece for 170 Leopard 2 battle tanks

December

Rheinmetall DeTec
Rheinmetall Defence Electronics is represented at the Interservice/Industry Training, Simulation and Education Conference in Orlando

Rheinmetall DeTec
Oerlikon Contraves attends the Dubai International Aerospace Exhibition

Rheinmetall
participates in the Investors Conference organized by ING BHF Bank

Rheinmetall DeTec
Oerlikon Contraves rated in its entirety by the renowned Brussels-based European Foundation for Quality Management and awarded the certificate Recognized for Excellence in Europe

Rheinmetall DeTec
The German navy receives the first remote-controlled MLG 27 light naval gun, developed for close-range self-protection of battle ships and other smallish units at sea

Rheinmetall
completely redesigns and relaunches its website with new content at www.rheinmetall.com

Kolbenschmidt Pierburg
MSI Motor Service International announces that it is acquiring as of January 2, 2004, through its subsidiary MTS Motorenteile-Service, the engine parts businesses of E. Trost GmbH & Co. KG Generalvertretungen and PV Autoteile

Report of the Supervisory Board

The Executive Board's policy of prompt and direct information enabled the Supervisory Board to fully and properly perform the controlling and monitoring functions incumbent on the Supervisory Board under law, Rheinmetall AG's bylaws and the rules of procedure and thus to monitor the Executive Board's management and conduct of business.

Focal points of deliberations
In fiscal 2003, the Executive Board briefed the Supervisory Board at each of the six meetings (including two extraordinary ones) on Rheinmetall's position and development prospects on the various markets and presented a detailed status report on the current business situation, assets and capital, financial position and results of operations of the Group and its subsidiaries. Fundamental business policy issues and the current risk management results were discussed in depth. Executive Board transactions requiring approval were duly submitted for decision to, and approved by, the Supervisory Board.

At its April 7, 2003 meeting, the Supervisory Board approved the voluntary public offering to the minority stockholders of Kolbenschmidt Pierburg AG and, at its extraordinary meeting of July 22, 2003, consented to the merger of Aditron AG into Rheinmetall AG. Moreover, when meeting on September 18, 2003, the Supervisory Board dealt with the sale and transfer of Jagenberg AG. The go-ahead to dispose of the business operations of STN Atlas Marine Electronics GmbH was given at the Supervisory Board's extraordinary meeting of October 24, 2003.

High on the Supervisory Board's agenda for detailed deliberations were Rheinmetall's strategic, operative and structural development issues. The complex portfolio of shareholdings was resolutely aligned with strategic and/or financial parameters and consistently refocused on Rheinmetall's fortes. The priorities adopted in the process will mean a further sustained improvement of the Group's profitability.

Quarterly reports updated the Supervisory Board members between their scheduled meetings on the most recent economic and financial developments. Additionally, the Supervisory Board Chairman and the CEO were regularly exchanging information and ideas. At informal meetings, the Executive Board reported on major transactions and developments, outstanding events and forthcoming decisions.

Through reports and Executive Board information, the Supervisory Board was directly involved in all decisions of fundamental strategic import and material implications for the Group and thus able to satisfy itself of the due and proper conduct of business by the Executive Board.

After thorough deliberation and upon recommendation of an ad hoc group from among its members, the Supervisory Board resolved at its meeting on May 26, 2003, to substantially restate its own rules of procedure while, at the same time approving the rules for its audit, personnel and slate submittal committees in ways that conform with the recommendations of the German Corporate Governance Code.

Supervisory Board committees
Committees assist the Supervisory Board in its activities. At three meetings, the Personnel Committee conferred on issues and actions on the agenda for decision in 2003. The Finance Committee met on April 3, 2003, with the statutory auditors to deliberate in depth on the upcoming approval of the separate and consolidated financial statements 2002. The Slate Submittal Committee, formed under the terms of Art. 27(3) German Codetermination Act ("MitbestG"), did not meet in the year under review. In line with the German Corporate Governance Code recommendations, the former Finance Committee was succeeded by a newly established Audit Committee, which met on November 12, 2003.

Corporate governance
The Supervisory and Executive Boards fully endorse the concept of responsible and transparent corporate governance and control aimed at enhancing shareholder value and modeled on German and international standards. In November 2003/February 2004, the two boards updated their declaration of conformity in accordance with the German Corporate Governance Code (as amended up to May 21, 2003) and Art. 161 German Stock Corporation Act ("AktG"). The full wording is reprinted on page 14 of this annual report and also publicly available on the Internet at ‹www.rheinmetall.com/cg.php›

Supervisory Board changes
In the wake of the divestment of Preh-Werke GmbH & Co. KG and STN Atlas Marine Electronics GmbH's operations, Egon Friedel and Erik Merks left the Supervisory Board as of October 31, 2003. Dr. Horst Girke and Gisela Walter stepped down from this Board as of December 31, 2003. The Supervisory Board thanks its previous members for their commitment and cooperation in Rheinmetall's best interests. On November 7, 2003, Hans-Peter Haug and Peter Winter, on January 22, 2004, Dr. Dieter Schadt, and on February 9, 2004, Harald Töpfer were appointed by the Düsseldorf Local Court of Registration pursuant to Art. 104 AktG as Supervisory Board members to succeed the resigned members for the latter's remaining term of office, i.e., up to the close of the annual stockholders' meeting that votes on the official approval of Supervisory Board acts and omissions for fiscal 2006.

Financial statements 2003
Rheinmetall AG's separate financial statements and the management report, which were prepared in accordance with the German

Commercial Code ("HGB"), and the consolidated financial statements as of December 31, 2003, and group management report, which in line with Art. 292a HGB were formulated in conformity with the IAS/IFRS, as well as the Executive Board's dependency report on affiliations were all (including the accounting system) examined by Düsseldorf-based PwC Deutsche Revision Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, the statutory auditors appointed for fiscal 2003 by the annual stockholders' meeting of May 27, 2003, in accordance with the Supervisory Board's audit engagement letter. An unqualified auditor's opinion was issued on both sets of financial statements.

In the scope of the risk management system audit under the terms of Art. 317(4) HGB, the statutory auditors were also required to assess whether the Executive Board had taken due steps for risk monitoring and installing an early risk identification system (ERIS) in line with Art. 91(2) AktG in order to identify in good time any developments that might jeopardize the Company's continued existence as a going concern. The auditors confirm that the system and tools installed are suitable for these purposes and that the management report on Rheinmetall AG and the Group presents a true and fair view of the risks of future developments.

At its March 22, 2004 meeting, the Supervisory Board's Audit Committee discussed on the basis of the audit reports all relevant details with the attending auditors who, in turn, briefed the Committee on the annual audit in general, certain focal areas, and their conclusions. The Audit Committee members recommended that the Supervisory Board adopt the separate and consolidated financial statements.

The Company's and the Group's annual accounts documentation, as well as the pertinent audit reports had been submitted to all Supervisory Board members early enough to ensure thorough and careful scrutiny. The documents were discussed in detail at the Supervisory Board meeting held on March 25, 2004, to adopt the financial statements. The audit report signatories attended this annual accounts meeting, reported on major audit conclusions and were available for additional information. No objections were raised.

The Supervisory Board agrees with the audit conclusions and reviewed on its own the separate and consolidated financial statements, the management reports on Rheinmetall AG and the Group, as well as the Executive Board's proposal for profit appropriation. According to the final results of this review, the Supervisory Board saw no reason to object.

At its meeting of March 25, 2004, the Supervisory Board approved the separate and consolidated financial statements for the fiscal year 2003 as submitted by the Executive Board; the annual financial statements for 2003 are thus adopted under the terms of Art. 172 AktG.

The Supervisory Board concurs with the management reports on Rheinmetall AG and the Group, including the assessment of Rheinmetall's further development. Moreover, the Supervisory Board agrees with the Executive Board's proposal for the appropriation of net earnings, which is based on a cash dividend of €0.64 per share of common, and €0.70 per share of preferred, stock and will be submitted to the annual stockholders' meeting for voting.

The Executive Board submitted to the Supervisory Board the dependency report concerning affiliations for fiscal 2003 according to Art. 312 AktG and the pertinent report of the statutory auditors. The Supervisory Board examined the report of the Executive Board and concurs with it, as with the results of the examination by the auditors, who issued the following opinion on the Executive Board's dependency report concerning affiliations:

"Based on our examination, which we performed with due professional care, and on our evaluation we certify that

1. the facts stated in the report are valid;

2. the Company's consideration for the legal transactions referred to in the report was not unreasonably high or disadvantages were compensated for."

After reviewing the final results of its own examination, the Supervisory Board found no reasons for objections to the Executive Board's concluding statement in the report on affiliations for fiscal 2003.

The members of the Supervisory Board thank the customers of all Rheinmetall companies and the stockholders for the trust they have placed in Rheinmetall. The Supervisory Board likewise thanks the Executive and Management Boards as well as all the employees for their dedicated efforts, their close personal commitment, and their valuable contributions in the best interests of Rheinmetall and its stockholders.

Our special thanks go to Dr. Ernst-Otto Krämer, Executive Board member of Rheinmetall AG and for many years CEO of Rheinmetall DeTec AG. After over 33 years with the Rheinmetall Group and almost a complete decade in command of its Defence sector, Dr. Krämer has now retired and left the Group as of February 29, 2004. The Supervisory Board thanks Dr. Krämer for his strong personal commitment in performing a variety of duties within the Group and most notably for his outstanding efforts in the interests of the Rheinmetall DeTec Group which he has grown into an economically solid and successful company in the European market for land forces technology.

Düsseldorf, March 25, 2004
The Supervisory Board

Klaus Greinert
Chairman

Letter from the Executive Board

Dr. Gerd Kleinert Klaus Eberhardt Dr. Herbert Müller

Dear Stockholders, Customers, and Friends
of the Rheinmetall Group:

The year 2003 was a rewarding period for Rheinmetall!

- Rewarding for our stockholders who benefited from a 115-percent price gain.
- Rewarding for the Group that managed to raise its like-for-like adjusted results of operations by 20+ percent and again slash net financial debts, this time by 24 percent. What's more, the portfolio-pruning program is largely finalized with the sale of further subsidiaries and business units worth almost one billion euros in sales plus the repurchase of minority interests in our subsidiaries.
- And, last but not least, rewarding for our customers who enjoyed the advantages of further improved products through numerous innovations and engineering advances from Rheinmetall.

Our thanks go to all the employees that have made this period so rewarding. Our thanks likewise to the employee representatives for their constructive support during the Group's necessary restructuring programs whose outcome will help safeguard jobs within the Rheinmetall Group despite such economically troubled times.

Group restructuring completed

The Group's rebuilding program drew to a close in the course of 2003 and early 2004, with only a few finishing touches left. "Impressively successful in restructuring the Group," so say financial analysts. "Rheinmetall has successfully completed its metamorphosis from a sales-driven, diversified industrial conglomerate into a value-emphasizing, closely focused group," states a study on the subject of our group. And again: "Rheinmetall has been one of the biggest restructuring stories in corporate Germany."

Indeed, Rheinmetall has vastly simplified its structures and decimated its holding company costs. For the investor community, Rheinmetall has grown a lot more transparent: of the erstwhile six sectors, two remain: Automotive and Defence.

Since 2000, this concentration on the two core sectors has meant heavy divestments which aggregate over €2 billion in sales. Despite this, thanks to an average organic growth of over 5 percent annually and a number of calculated acquisitions, total sales had by the end of 2003 slipped but slightly. More important, profitability (in EBIT margin terms) has advanced from 1.5 to 4.8 percent during these years of restructuring.

Concurrently, we succeeded in slashing our net financial debts, in 2000 easily in excess of €1 billion, to €230 million in fiscal 2003, even though during the past years we spent around €500 million in repurchasing minority interests in some of our subsidiaries.

The major surgery undergone by the Rheinmetall Group and accelerated by the decision to sell off the entire Electronics sector last year, makes it difficult to compare key performance figures from one year to the next. This annual report 2003, which you are reading, presents such comparability at important points in order to facilitate an objective assessment of the Group's progress.

Profitability clearly up

The 2003 EBIT reduction is attributable to the 2002 gain from the sale of Heimann Systems (Security) and the departure of Naval Systems from the Defence sector which together account for operating profit contributions lost in 2003 of around €40 million. Still, the adjusted EBIT for 2003 exceeded the year-earlier magnitude. Adjusted for all consolidation group changes and hence comparable to 2002 (current shareholdings portfolio restated for 2002), Rheinmetall's 2003 like-for-like EBIT was up by €42 million, largely due to the successful restructuring of the core Automotive and Defence sectors.

Besides the improved results of operations, the sharp reduction in debts has meant a decrease in net interest expense of €18 million. And just as important: through the repurchase of numerous minority interests, third parties in 2003 pocketed some €23 million less of our net income. Now and in future, this will mean greater leverage for Rheinmetall AG's stockholders who will be entitled to almost all of the Rheinmetall Group's net income.

The rewards of our restructuring efforts are most evident in terms of EpS, adjusted for both positive and negative nonrecurring effects. For the preferred stock, this has climbed from €1.38 in 2001 to €1.83 in 2002 to €2.85 in 2003, almost doubling inside three years.

Confident as to 2004

On the basis of our profitability drive and structural balance sheet improvement efforts during the past years we at Rheinmetall are altogether highly confident regarding the prospects for fiscal 2004. We expect each one of our nine Automotive and Defence units to turn in a profit. As to the Group as such, we must bear in mind that for 2004 and following the wave of disposals, we are faced with an entirely new sales and earnings base. Assuming a stable economy, Group sales will range around €3.5 billion. Like-for-like, this means that we are sticking to our organic growth of about 5 percent annually. The EBIT margin is again planned to rise. Moreover, one-off burdens caused by the meanwhile sold Jagenberg Group will no longer occur, these having eroded earnings by €31 million in 2003. The net financial result will show another improvement in 2004.

The Rheinmetall Group has set itself ambitious goals not only for 2004 but medium term, too. Over the next three years, we are budgeting an organic sales growth of at least 5 percent annually. And, given the healthy financial and cash situation, acquisitions designed to selectively strengthen core businesses are back on the agenda. Our midrange EBIT margin and ROCE benchmarks are 7 and 15 percent, respectively. As to our equity ratio, 25 percent is, in our view, a comfortably safe long-term haven for Rheinmetall.

As a sign of the Rheinmetall Group's much healthier financial and profitability state, the Supervisory and Executive Boards will propose to the stockholders' meeting that the bonus of €0.20 paid last year from the gains realized through the sale of Heimann Systems be added to the regular cash dividend which thus rises from €0.44 to €0.64 for the common and from €0.50 to €0.70 for the preferred stock.

The Group will continue to sharply focus on a further sustained advance in shareholder value. As far as we are concerned, we will do our utmost to make sure that 2004 is another rewarding year for our customers, our employees, and most especially, our stockholders.

Sincerely,

Klaus Eberhardt
CEO

Dr. Gerd Kleinert

Dr. Herbert Müller

Rheinmetall stock

Stock markets stage recovery

www.deutsche-boerse.com

Clouded by political and economic uncertainties, the leading stock markets at the start of 2003 resumed their downswing observable ever since 2000. Then, in the course of the second quarter, a recovery became evident on an international scale, with major indexes showing a turnaround. As the period proceeded, the recovery gained pace, spurred on by generally upbeat expectations regarding the global economy and propelled by the performance of the US economy.

Whereas Germany's leading index, the DAX, climbed in 2003 from 3,105 to 3,965 (up 27 percent), the MDAX shot up 44 percent, from 3,111 to 4,469 points.

Measured against its 2003 nadir of 2,647 on March 12, the gain was as much as 70 percent by year-end 2003.

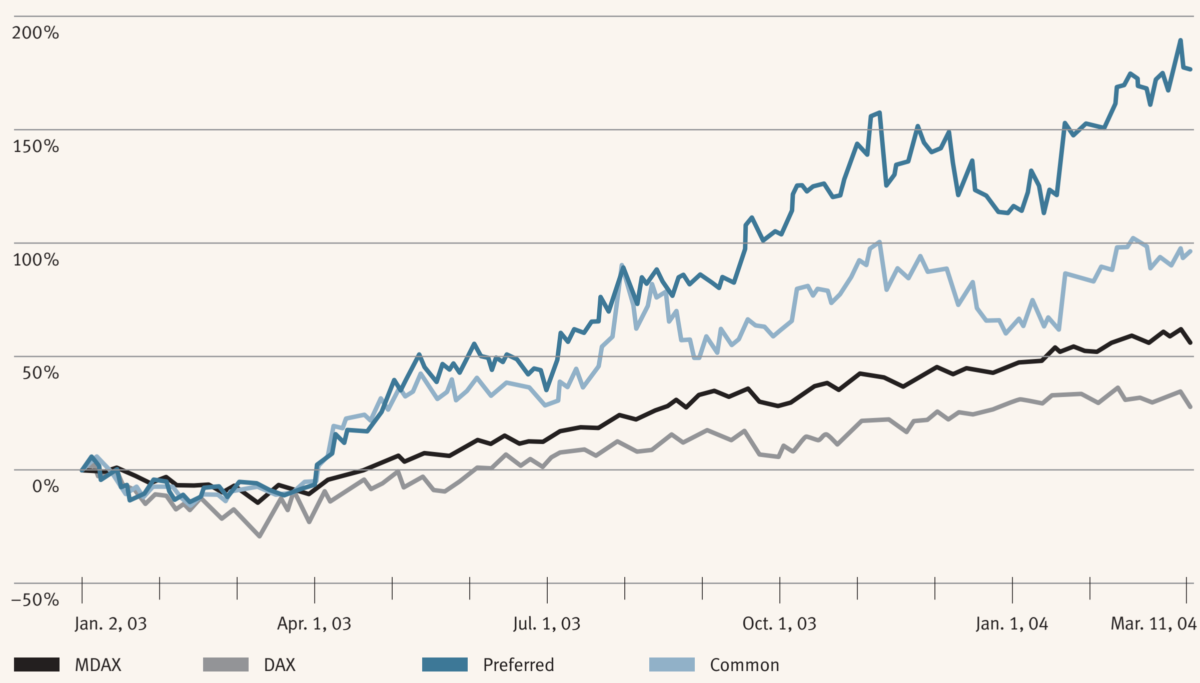
Following the re-indexing of the stock market in March 2003, Rheinmetall preferred stock within the Prime Standard is still among the MDAX which has shrunk from 70 to 50 members. Deutsche Börse has a ranking that determines index membership and in this, Rheinmetall preferred stock in December 2003 was placed 36th for market capitalization and 31st for stock turnover.

Rheinmetall preferred stock surges 115 percent

Rheinmetall stock had a very good year and qualified among the winners of the general upturn on the German stock market. In fact, this is the investor community's appreciation of the Group's efforts to restructure and focus more closely on shareholder value. The main elements of this refocus were to simplify the corporate structures by exclusively concentrating on the core Automotive and Defence sectors plus the repurchase of minority interests in a number of subsidiaries. The related substantial improvement in balance sheet ratios through a massive reduction in debts, enhanced profitability, and greater ownership and hence performance transparency, all found favor with the capital market.

Rheinmetall stock price trend compared to DAX and MDAX

January 2, 2003 to March 11, 2004



During 2003, Rheinmetall preferred stock prices ranged between €9.65 (annual low on February 13, 2003) and €28.86 (annual high on November 11, 2003). The preferred stock closed 2003 at €23.65 or 115 percent above the year-earlier €11.01. This gain easily outpaced those of the other key indexes.

The common stock advanced to €23.01 at December 30, 2003 (a gain of 56 percent). This stock's annual low was €12.45 on February 13, 2003, its year high €28.90 on November 11, 2003. These price surges meant that the Rheinmetall Group's market capitalization jumped from €463 million to meanwhile over €1 billion inside one year. On the year's final trading day, it had reached around €840 million. The total number of shares, preferred and common, is still in each case 18 million. The average daily trading volume (XETRA and Frankfurt) for the more liquid preferred variety grew from 35,500 in 2002 to 63,200 in the period.

Capital market manifests rising interest in Rheinmetall

The capital market has been following Rheinmetall's stock price trend with keen interest while, at the same time, carefully calculated and redoubled investor relations efforts succeeded in drawing the attention of many additional analysts and investors to Rheinmetall stock.

www.rheinmetall.com/coverage.php

In the course of fiscal 2003, the research departments of seven notable financial institutes started coverage of Rheinmetall stock. These are Deutsche Bank, Dresdner Kleinwort Wasserstein, Berenberg Bank, Bayerische Hypo- und Vereinsbank, ING BHF-Bank, Bankgesellschaft Berlin, and Equinet. Six of their analysts recommended "buy," the seventh "hold." The number of analysts that have earmarked the Rheinmetall Group for regular review has thus climbed to nigh 20.

A large number of information sessions aimed at gratifying the thirst for details of the capital market were organized to outline and explain the situation inside the Company. These included group participation at five investor conferences in and outside Germany, five self-organized events as well as regular teleconferences coinciding with the publication of the quarterly accounts and attended by numerous (inter)national analysts and fund managers.

Eight road shows were staged at major European financial centers and over 100 interviews organized with (chiefly foreign) fund managers.

In its relationship with the investor community, Rheinmetall is increasingly turning to the Internet, one advantage being equal treatment and opportunities for all. The important corporate presentations, publications and information related to Rheinmetall stock are viewable in their entirety at www.rheinmetall.com which also had, for the first time in 2003, factbooks with an illuminating account of the Automotive and Defence sectors.

Ownership structure 2003: Private individuals predominant

As in previous years, Rheinmetall carried out a poll among the most important depositary banks in the spring of 2003. Compared with the year-earlier figures, the proportion of shares held by majority stockholder Röchling Industrie Verwaltung (RIV) is unchanged, this latter holding a 42.1-percent stake in Rheinmetall AG's capital stock, viz. 73.7 percent of the common, and 10.5 percent of the preferred, stock.

Of the 95+ percent of all stock researched, around 79 percent is held in German accounts, the rest abroad. In the case of the preferred stock and virtually unchanged over the previous year, around 75 percent is deposited in Germany, of the common stock some 82 percent.

The preferred shares held abroad are about 90 percent in the portfolios of institutional investors, chiefly in Britain, Switzerland, Luxembourg, and the USA.

Rheinmetall stock

Among the owners of preferred stock in Germany, besides RIV the vast majority are still private individuals (accounting for over 8 million shares) while institutional investors hold some 2.5 million shares. This means that the number of shares owned by institutional investors rose by around 0.7 million versus the 2002 poll. Given the much keener interest on the part of such investors, especially Anglosaxon, the proportion is likely to show a significant gain at the start of 2004.

Rheinmetall's preferred shares were held in around 20,300 securities accounts, the common variety in some 4,600, mainly in Germany. Foreign stockholders have around 600 accounts with Rheinmetall shares.

ROCE: the prime benchmark

Rheinmetall is committed to enhancing shareholder value and hence the related ratios, most especially ROCE, are important signposts in the control and command of the Group.

The outcome of the shareholder value enhancement steps is reflected in the EpS figures. On the basis of figures adjusted for nonoperating one-time effects, earnings per share show a steady rise over a three-year period.

Performance of preferred stock *per share, in €*

	2001	2002	**2003**
EpS before goodwill amortization	0.62	6.87	1.78
Adjusted EpS before goodwill amortization	1.09	7.95	2.62
EpS after goodwill amortization	1.38	1.83	2.85
Cash flow [1] per share from operating activities	8.71	9.47	8.36
Operating free cash flow per share	0.83	2.58	2.72

[1] *according to cash flow statement*

For a number of years now, the Group has been repurchasing minority interests in Rheinmetall AG's subsidiaries. Meanwhile, except for €5 million (down from €28 million), almost all of the Group's net income accrues to Rheinmetall AG's stockholders.

Dividend rise proposed

www.rheinmetall.com/dividende.php

For fiscal 2003 and on the basis of the net income reported, Rheinmetall will propose to the annual stockholders' meeting a cash dividend of €0.64 per common share and €0.70 per preferred share. Consequently, last year's bonus of €0.20 (for the sale of Heimann Systems) is now fully included in the dividends. Related to the 2003 closing prices, these dividends will produce a yield of 2.8 and 3.0 percent for common and preferred stock, respectively.

Rheinmetall on the debt market

Diversified finance

Against the backdrop of the financial markets flashing many signals of uncertainty, Rheinmetall started a number of years ago to consistently diversify its sources of debt capital over and above the scope of traditional bank loans. The Group can meantime tap several short- and long-term sources of finance.

Since 2002, Rheinmetall has used a €500 million commercial paper (CP) program to issue short-term debt instruments, which have met with enthusiastic market response. The syndicated 5-year €400 million credit facility approved in 2002 is used as a back-up line in connection with the CP program. Quick funds can now be raised additionally from the credit or the CP markets.

In 2001, a 5-year €350 million corporate bond issue was floated as a long-term financing instrument for the Group. In addition, Rheinmetall again launched a €127 million asset-backed securities (ABS) program in 2003.

The Rheinmetall Group has thus broadened its investor base by increasing its independence of individual investor groupings while ensuring the best possible maturity range for debt capital and securing long-term financial resources.

Uptrend of the Rheinmetall bond on the secondary market

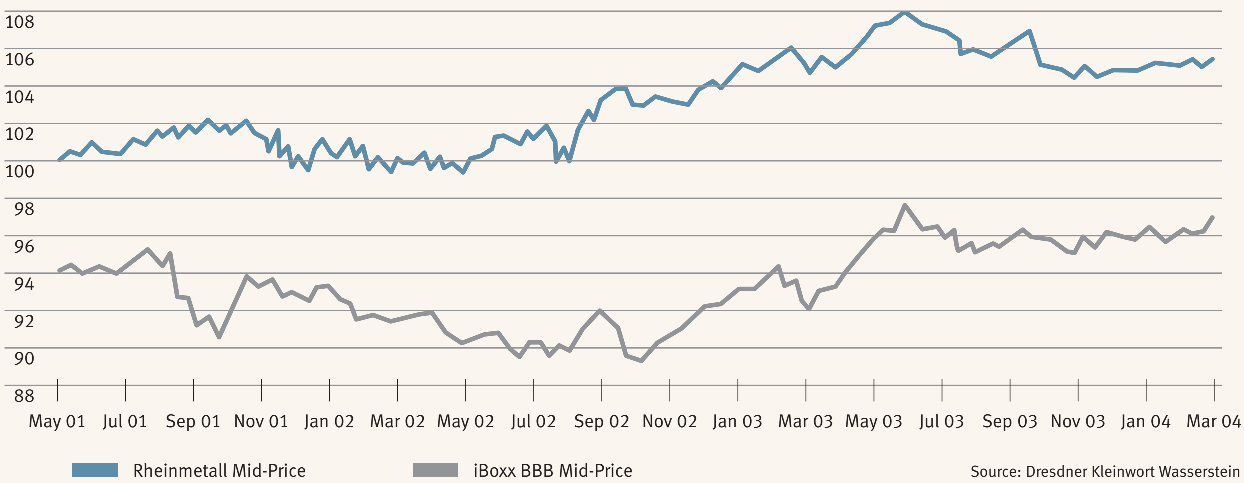
Fiscal 2003 proved to be a very good year for euro-denominated corporate bond issues, basically in view of low interest rate levels and a generally strong demand by investors, this narrowing the credit spreads appreciably and boosting bond prices, especially in the BBB-rated segment.

The 6.125-percent Rheinmetall bond issued in May 2001 upheld its position in 2003 amid a friendly market. Throughout the year 2003, the price of this bond remained above the level of iBoxx BBB, a segment index that reflects comparable investments. Toward year-end, Rheinmetall's bond credit spread more than halved in comparison to the year before.

As of December 31, 2003, the bond was quoted at 104.71 percent (2001 issuance price: 99.54 percent); it is traded at the Luxembourg Bourse under WKN 677 862 6 and ISIN DE 000 677 862 6.

Rheinmetall bond price trend versus iBoxx BBB

May 2001 to March 2004



Source: Dresdner Kleinwort Wasserstein

Asset swap spread based on the Rheinmetall bond bid price BBB segment

Corporate governance

Rheinmetall AG fully endorses the concept of responsible and transparent corporate governance and control aimed at enhancing shareholder value. Even the previous practice largely conformed to the recommendations and suggestions of the German Corporate Governance Code (the "Code"). The confidence placed by (inter)national investors, stakeholders and the general public in the governance and control of the Rheinmetall Group will be further promoted since Rheinmetall sees corporate governance as an ongoing process to refine governance and control practices in the wake of new experiences and regulations, as well as new developments in national and international standards.

www.corporate-governance-code.com

www.rheinmetall.com/cg.php

On December 20, 2002, the Executive and Supervisory Boards issued their first declaration of conformity pursuant to Art. 161 AktG according to which Rheinmetall AG had adopted the Code's recommendations subject to three exceptions. In fiscal 2003, action was taken to substantially meet all requirements and thus eliminate the exceptions.

The Code was further developed and extended by May 21, 2003, to cover several new items. The recommendations of the amended Code which to date have not yet been implemented by Rheinmetall are described in the declaration of conformity of Rheinmetall AG's Executive and Supervisory Boards as reproduced below and published in December 2003/February 2004 on the Company's website for public access whenever required:

Declaration of conformity pursuant to Art. 161 AktG on the compliance by Rheinmetall AG with the German Corporate Governance Code

Pursuant to Art. 161 AktG, Rheinmetall AG's Executive and Supervisory Boards declare in respect of the recommendations of the German Corporate Governance Code Government Commission:

Rheinmetall AG observes the recommendations of the German Corporate Governance Code as amended up to May 21, 2003, and published in the digital Federal Gazette, subject to the following exception:

– The remuneration paid to each individual Executive and Supervisory Board member (4.2.4 and 5.4.5 of the Code, respectively) will not be disclosed in the notes to the consolidated financial statements.

Since the preceding declaration of conformity issued in December 2002, Rheinmetall AG has adopted the recommendations of the Code as amended up to November 7, 2002, subject to the following exceptions:

– Up to May 26, 2003, no procedure had been implemented that would bind Supervisory Board members to record, report to the Supervisory Board (5.5.2 of the Code) and disclose in the Supervisory Board report to the annual stockholders' meeting (5.5.3 of the Code), any conflicts of interest.

  At its May 26, 2003 meeting, Rheinmetall AG's Supervisory Board approved its new rules of procedure, which have since complied with the recommendations of the Code in this respect.

– Regarding Supervisory Board remuneration, membership in Supervisory Board committees had not been separately compensated for (5.4.5 of the Code). At its meeting of November 27, 2003, the Supervisory Board resolved that, starting from fiscal 2003, committee membership will be remunerated accordingly; this resolution will be submitted to the May 2004 annual stockholders' meeting, which will vote on an amendment to the Company's bylaws.

– In fiscal 2003, the publication deadlines recommended in the Code for the consolidated financial statements and the interim reports were not yet observed but compliance as from 2004 with this recommendation has been ensured (7.1.2 of the Code).

Executive Board

www.rheinmetall.com/satzung.php

The Executive Board's duties and powers are defined by law, Rheinmetall AG's bylaws, and the Executive Board rules of procedure. In 2003, the Executive Board had four members who, though acting on their own in the scope of the segment responsibilities assigned to them, are obligated to subordinate segment-related interests throughout to the overall good of Rheinmetall as a whole. The CEO chairs the Executive Board and coordinates its work.

In the notes to the consolidated financial statements, aggregated details provide meaningful information about the remuneration of Rheinmetall AG's combined Executive Board, broken down by fixed, performance-related and shareholder value-enhancing incentive components. The information that concerns stockholders relates to the Board in its entirety, its members sharing responsibility for the way the Group is run. These aggregate figures contain all the data needed to assess pay/performance adequacy and whether the breakdown by fixed and variable pay components is suitable for sufficiently motivating the Executive Board members.

The compensation structure is determined by the Supervisory Board at a reasonable level and on the basis of a personal performance assessment, with due regard to any other compensation paid by the Group. Assessment criteria for defining a reasonable remuneration of Executive Board members mainly include each member's responsibilities, contribution and personal performance, as well as the economic situation, success and future prospects of Rheinmetall on industry comparison. The remuneration is fixed at a competitive level consistent with international market conditions for highly qualified executives, its amount and structure being modeled on the compensation paid by comparable German or foreign corporations.

The target income breaks down into a 60-percent fixed, and 40-percent variable, portion. Additionally, an incentive program has been installed that is pegged to the absolute annual increase in the Rheinmetall Group's shareholder value. This program is not linked to Rheinmetall AG's stock price but solely to the absolute enhancement of the "fundamental equity value" on the basis of defined economic indicators.

The Supervisory Board Chairman will brief the annual stockholders' meeting on May 11, 2004, on the basic elements of Executive Board remuneration, which have also been outlined on the Company's website.

In the year under review, no loans or advances were granted to Executive Board members.

The Company has taken out a D&O policy (Directors' & Officers' liability insurance, including consequential loss) with a reasonable deductible for its Executive Board members.

Corporate governance

Supervisory Board

The Supervisory Board approved at its meeting on May 26, 2003, its substantially restated rules of procedure and the rules for its personnel, audit and slate submittal committees. The former finance committee has been succeeded by a newly established audit committee.

The committees, whose members are equally stockholder and employee representatives, deal with complex issues and prepare resolutions for submittal to, and adoption by, the plenary Supervisory Board meeting, such as:

Personnel Committee
This committee is in charge of all Executive Board personnel matters and represents the Company when dealing with Executive Board members. Moreover, it is responsible for preparing the new or reappointment of Executive Board members, gives the plenary Supervisory Board recommendations and, together with the Executive Board, works out long-term succession plans.

Audit Committee
The Supervisory Board has established an audit committee to perform the functions and duties mentioned in 5.3.2 of the Code (as amended up to May 21, 2003). In addition, this committee prepares Supervisory Board resolutions in connection with capitalization moves and the adoption of annual financial statements, besides monitoring the finance structures within the Rheinmetall Group.

Slate Submittal Committee
This committee, whose establishment is prescribed by the German Codetermination Act, submits a slate of potential Executive Board candidates to the plenary Supervisory Board if the specified majority for the appointment of Executive Board members does not suffice.

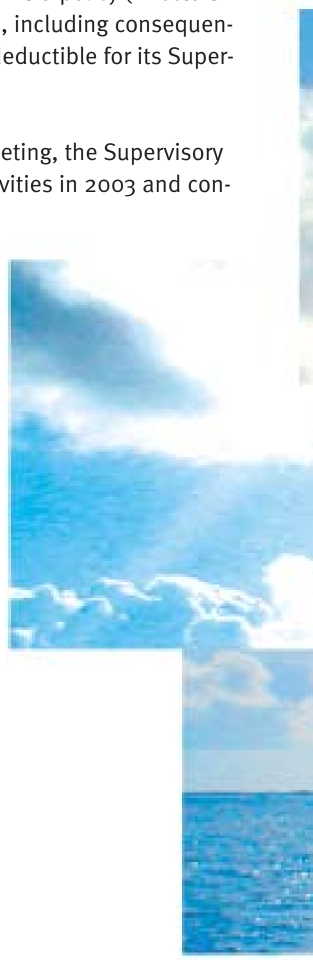
The Supervisory Board's remuneration includes fixed and variable fees, the latter depending on distributable dividends. The current fee system of Rheinmetall AG's Supervisory Board is detailed in Art. 13 of the bylaws. According to 5.4.5 clause 1 of the Code, chairmanship and committee membership should also be reflected in the fees; this, however, requires the bylaws to be amended accordingly. The Supervisory and Executive Boards have approved a proposal to the annual stockholders' meeting for voting on May 11, 2004, that the Supervisory Board fee system be redesigned with retroactive effect for fiscal 2003 to ensure that it complies with the recommendations of the Code as amended up to May 21, 2003.

An inquiry among the Supervisory Board members indicated that there were no conflicts of interests under the terms of Clauses 5.5.2 and 5.5.3 of the Code.

In the year under review, no loans or advances were granted to Supervisory Board members.

The Company has taken out a D&O policy (Directors' & Officers' liability insurance, including consequential loss) with a reasonable deductible for its Supervisory Board members.

At its November 27, 2003 meeting, the Supervisory Board dealt with its own activities in 2003 and conducted an efficiency audit.



Transparency

Pursuant to Art. 15a German Securities Trading Act (“WpHG”), the Executive and Supervisory Board members of Rheinmetall AG have been obligated to disclose their purchase or sale of any Rheinmetall stock. Upon inquiry, the Company did not receive any such notice of purchase or sale, nor did any reportable shareholdings exist under the terms of 6.6 of the Code.

Worldwide unique protection against dynamic precision weapons: the Mass naval defence system

Communication and marketing

Ready media reception

Fiscal 2003 was a period in which the media were absorbed by events at Rheinmetall, chiefly on account of the economic rewards harvested from the Group's restructuring programs, surging stock prices, and the strategic decision to focus exclusively on the two core sectors of Automotive and Defence. Likewise eliciting a broad resonance were various megacontracts as well as the production start-up of the new Puma infantry tank at Rheinmetall DeTec or Pierburg's premiere of a new electric coolant pump designed to obsolete the traditional V-belt while adding an important contribution to the conservation of resources and the reduction of emissions.

In the field of coolant pumps Pierburg is the market leader in Europe

In the course of 2003, the Rheinmetall Group addressed a wide variety of information needs with altogether 215 press releases for the business and trade press along with almost 40 interviews given by executive and management board members plus 27 events staged for the press.

Not only did Rheinmetall achieve quality coverage, the media also responded positively to the general tenor of the corporate strategy. Instances include headlines like "Diet delivers results at Rheinmetall" (Die Welt), "Rheinmetall gains financial stature" (Financial Times Deutschland), and "Stock exchange impressed by Rheinmetall" (Börsen-Zeitung).

Enthusiastic media echo

Börsen-Zeitung commented on the occasion of the annual accounts press conference held in April 2003:

“Now that the rebuilding program rolled out in 2000 is complete, CEO Klaus Eberhardt can commence with the harvesting phase of his Clear Directions strategy and set his sights on new targets... Inside three years, companies worth altogether €1.1 billion in sales have been jettisoned yet the volume of business has not shrunk during this time but even advanced slightly thanks to vigorous organic growth (€0.8 billion).” Börsen-Zeitung, April 11, 2003

The daily *Die Welt* came to a similar conclusion:

“Three years back, Eberhardt had prescribed his Clear Directions strategy for what was then a jumbled technology group—and now he is able reap the rewards. Eberhardt presented a neatly structured group with solid earnings ability, low indebtedness, and better-than-average growth rates.”
Die Welt, April 11, 2003

Notwithstanding the still hostile economic parameters, Rheinmetall continued in 2003 to make solid economic progress on the basis of the successful restructuring. *Handelsblatt* commented as follows:

“Rheinmetall is increasingly able to reap the rewards of its corporate restructuring efforts. Costs are sinking and debts finally returning to healthy proportions. Behind all this is the transformation from a sales-driven industrial conglomerate that had repeatedly confused investors with alarming news about one of the many subsidiaries, into a growth-focused group.” Handelsblatt, August 19, 2003

The decision to shed the Electronics sector was likewise perceived by the media as a logical step within the Executive Board’s overall strategy. The *Frankfurter Allgemeine Zeitung* summed this up as follows in November 2003:

“On the way to becoming purely and simply a defence and auto group, Rheinmetall AG achieved in 2003 much improved profitability in these two core businesses. This found its appreciation in the stock market’s echo to the interim report.” FAZ, November 18, 2003

Successful trade fair attendance

Attending trade fairs is a firm fixture of the communication and marketing strategies of all Rheinmetall Group companies. Besides providing an opportunity to showcase innovations, such attendance also offers the advantage of contact with customers, markets, and media. During 2003 Rheinmetall companies presented their products and services at worldwide 75 trade fair and symposiums. Major events for Automotive were the Frankfurt Motor Show, the Detroit SAE, and the Paris Equip’ Auto; for Defence IDEX in Abu Dhabi, DSEI in London and IDEF in Ankara.

General economic conditions

Beginnings of a world economic recovery

The year 2003 was characterized by two differing economic sentiments. During the first six months, it was above all the Iraq war and concerns about a resulting global economic crisis that led to general uncertainty. This situation was measurably reflected in a pronounced lack of spending propensity on the part of the corporate community, reluctance to consume on the part of private households, and bearish capital markets. During the second half of the year, this trend reversed. Since the fourth quarter of 2003 at the latest, there has been a relatively broad consensus that the world economy is entering a new upward phase.

The starting point for this shift of opinion was above all the US economy, which in Q3/2003 showed the strongest growth for almost two decades. In addition, many US economists forecasted a recovery for the US labor market. This encouraging news clearly left its mark on the mood of consumers. All in all, the US recorded economic growth of 3.1 percent in 2003, according to provisional estimates.

A comparable, albeit weaker, trend was observed in the eurozone. Following a first six months of contracting economic output and somewhat pessimistic forecasts, a turnaround was discernible in Euroland in the third quarter, fueled by strong exports—despite the euro's rise—albeit against a background of continued stagnating domestic demand. The return to the growth path also brought about a marked improvement in the business climate, with all sectors of the economy, except for the retail trade, contributing to this brighter outlook. According to initial estimates, an 0.4-percent rise in gross domestic product is predicted for the eurozone in 2003.

As in previous years, Asia registered the strongest economic momentum in 2003. Unlike in past years, even Japan is expected to return to positive territory again, recording industrial growth of 2.1 percent in 2003. The favorable trend continued unabated in China where the growth rate of the economy exceeded 8 percent in 2003. Economic indicators were also showing a clear upward trend in Russia with expansion at more than 6 percent.

Encouraging business indicators for Germany

www.ifo.de

During the past year, the German economy found it much more difficult to gather momentum again. Following two years of stagnation, gross domestic product in the first six months of 2003 was slightly down on the preceding year. Signs of a recovery were initially based on "soft" indicators such as the IFO business climate index, which during the course of the year reached its highest level since January 2001.

In the third and fourth quarters, gross domestic product returned to show an increase for the first time, with order intake in particular advancing. Especially the upturn in the USA—in spite of the euro's sharp rise against the dollar—filled the order books of German exporters. Accordingly, the economic report presented by the OECD in the fall of 2003 assumed that export trade above all would supply Germany with thrust, domestic demand remaining muted for the time being. Over the entire year, the German economy contracted slightly, with negative growth of 0.1 percent.

In general, the beginnings of an economic recovery in world markets impacted favorably on the automotive and defence sectors of relevance to Rheinmetall. The situation in the various sectors, however, varied according to industry and region.

No uniform trend in the automotive industry worldwide

The state of the international motor vehicle industry was clearly marked by several special factors in 2003. According to the estimates available to date, 58.0 million passenger cars and light commercial vehicles (LCV) were manufactured worldwide, up from 57.1 million units in 2002. This 1.6-percent production rise was chiefly due to production gains in Asia, apart from Japan.

In NAFTA (USA, Canada, Mexico), automobile production declined by about 3 percent to 15.9 million vehicles despite an economic rebound and generous discounts, especially in the USA. US manufacturers were not able to capitalize on their currency advantages in 2003, with the Big Three (General Motors, Ford, and Chrysler) losing further home turf market shares to foreign carmakers.

The car industry in Western Europe saw its production figures decline marginally by 0.8 percent to 16.8 million units in 2003, although the shrinkage was much less than the pessimistic annual forecasts for Western European automobile production in 2003. In key European auto markets, most notably in France and Italy, production was down on the preceding year. During the period under review, the production of passenger cars and LCVs in Germany fell for the second successive year owing to weak demand to 5.3 million units, representing a drop of 0.6 percent.

The economic upturn in Japan was not yet reflected in the production of passenger cars and LCVs, with Japanese auto production receding by 1.7 percent to 9.7 million units. There was no end to the demand and production boom in China, on the other hand, where production—up 40 percent to 3.6 million vehicles in 2003—again surged. In fact, China ranked fourth among the world's leading vehicle manufacturers in 2003.

In general, the Automotive sector with its modules and systems expertise managed as in the previous year to buck the overall somewhat subdued level of business activity in the car industry. Particularly helpful factors were the trend toward more diesel engines together with increased endeavors to reduce fuel consumption and emissions. For example, the proportion of diesel passenger cars in Western Europe rose to over 42 percent (up from 40 percent). In certain countries, Austria for example, the proportion of diesel vehicles among new registrations actually exceeded 70 percent. The focus on aluminum and increasingly on magnesium as lightweight components as well as Kolbenschmidt Pierburg's expertise in the growth segment of mechatronics (mechanics/electronics) also impacted favorably. Last but not least, involvement in new car models with buoyant production and sales figures also strengthened Kolbenschmidt Pierburg's position in 2003.

Defence technology profiting from increased security requirements

www.bmvg.de/ministerium/haushalt

Compared with other sectors, the defence technology business is affected to a lesser extent by the prevailing economic environment, depending on longer-term trends in national budgets besides being generally based on comparatively long product life cycles.

Against the rewritten global security scenario and due to the greatly increased number of internationally coordinated military and humanitarian missions, especially involving NATO forces, the basic external environment in which the Defence sector operates improved further. In addition, prompted by the new deployment scenarios, the armed forces of many countries are undergoing transformation, a process which entails changed matériel requirements. Even if the existing equipment is still being used, the defence technology industry is facing new challenges worldwide.

In 2003, the German armed forces initiated and implemented the initial steps in the direction of these changes, which are also due to be reflected for the first time in procurement planning as from 2005. The modernization of ordnance is directed primarily at internationally deployable mobile vehicles, the protection of soldiers on missions, the growth in command and reconnaissance components, and at bringing existing hardware into line with prevailing international standards.

At €24.4 billion, the German defence budget, which continues to be of paramount importance for the Defence sector, remained essentially unchanged in 2003, increases having been announced only from 2007. Of the total budget, matériel spending and R&D accounted for €5.0 billion as in the previous year. This means that again much less than 25 percent of the total budget is available in the national market for modernizing the equipment of the German armed forces. However, the German defence ministry is sticking to its objective of raising defence budget expenditures to 30 percent.

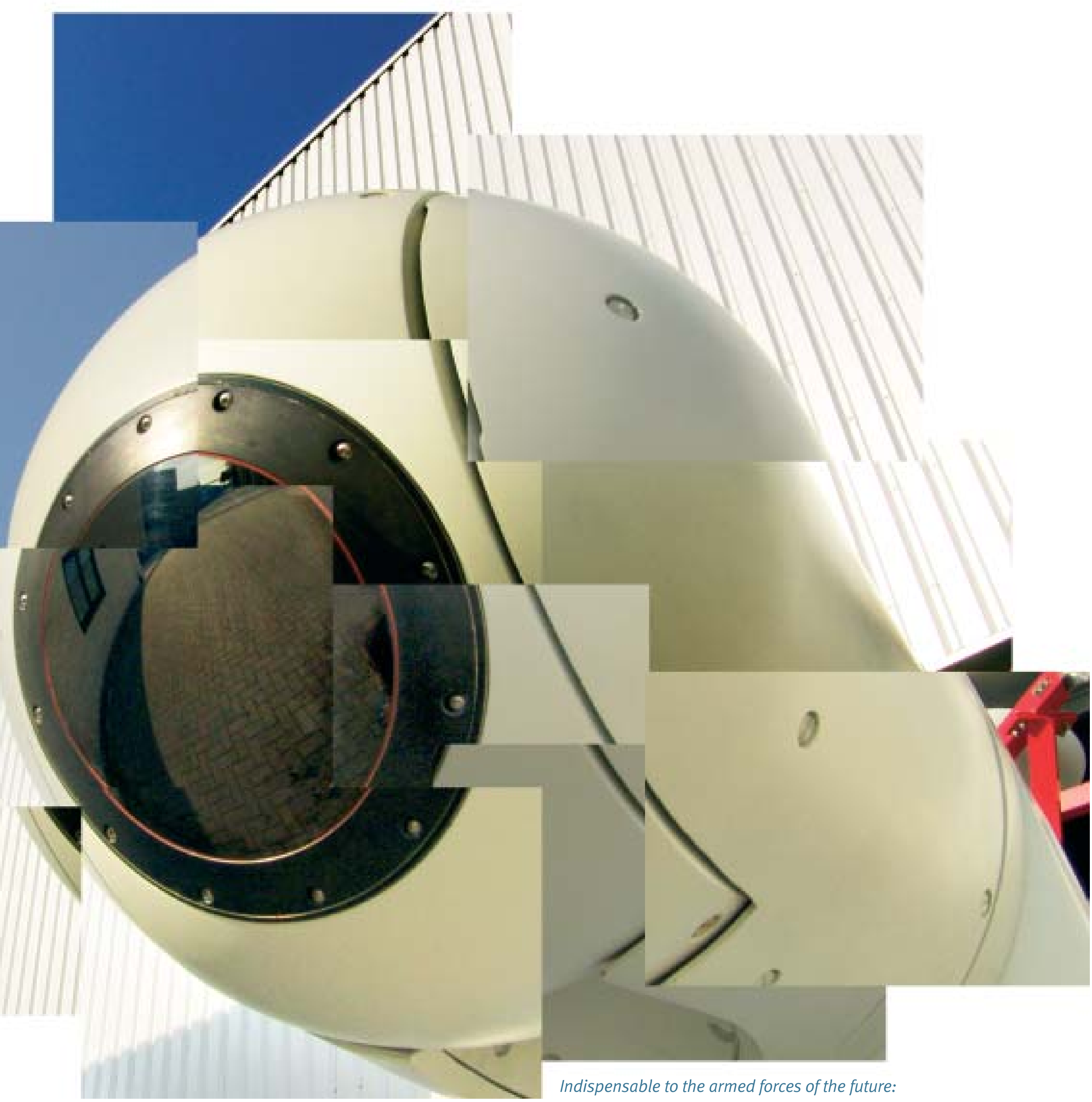
General economic conditions

In key European NATO states, such as France or Great Britain (€32.4 billion and €36.8 billion or 30 and 40 percent, respectively), the proportion of the respective defence budget earmarked for new matériel spending is well above the comparable German level.

Internationally, the trend toward rising arms expenditure that started in the late 1990s persisted during the year under review. In 2003, some US$800 billion was spent on armament worldwide, with the major industrial nations accounting for about 70 percent of this total. The highest rise in military spending was recorded in Central and Eastern Europe, Africa and Southeast Asia as well as the Middle East.

In view of national and international developments, Defence will press ahead in its efforts to access foreign markets and further lift the share of exports by exploiting worldwide market potentials. In reward for these efforts, the Rheinmetall DeTec Group succeeded in upping its non-German share of sales from 56 to 57 percent in 2003.

During 2003, Rheinmetall DeTec benefited above all from the rising demand for air-lifted and highly mobile armored vehicles. Additionally, the gaining importance of military reconnaissance through drones, for example, and the use of defence electronics impacted positively. In these growth segments, the Defence sector is a market-leading player on the cutting edge of technology. One important factor in the Defence sector's success is the prospect of long-term value added especially with military vehicles. Product life cycles of up to 30 years make it possible to add value beyond national development and production, such as through follow-up orders for export or maintenance and repeated product enhancements in some cases.



*Indispensable to the armed forces of the future:
the KZO unmanned reconnaissance system*

The situation of the Group

Rheinmetall Group indicators *€ million*

	2001	2002	2003
Net sales	4,603	4,571	4,248
Order intake	5,033	4,840	4,128
Order backlog (Dec. 31)	4,113	4,165	3,143
Employees (Dec. 31)	27,828	25,949	20,888
EBIT	195	392	204
EBT	84	290	120
Average capital employed	2,224	1,953	1,661
EBIT margin *in %*	4.2	8.6	4.8
ROCE *in %*	8.8	20.1	12.3

The following adjusted indicators can be derived from adjusted EBIT, cf. Note (30) to the consolidated financial statements:

	2001	2002	2003
Adjusted EBIT [1]	192	213	223
Adjusted EBIT margin *in %*	4.2	4.7	5.2
Adjusted ROCE *in %*	8.6	10.9	13.4

[1] *cf. Consolidated financial statements on page 92*

Major events in fiscal 2003

The program of optimizing the Group's portfolio in pursuit of enhanced shareholder value on a sustained basis was again taken further forward in 2003.

STN Atlas Elektronik GmbH, the joint venture belonging to Rheinmetall DeTec AG and BAE Systems Deutschland GmbH, was divided into two companies with effect from August 1, 2003. Atlas Elektronik GmbH, now integrated into BAE Systems, will focus in future on the maritime activities of the previously jointly run company, while Rheinmetall Defence Electronics GmbH with its land, air and simulation systems operates in the field of land forces equipment. The aim of this restructuring process is to consolidate the Defence sector's successful strategic position as Europe's leading supplier of land forces ordnance while further enhancing the company's profitability within the Rheinmetall DeTec Group by consistently improving its operational efficiency.

www.rheinmetall-de.com

With the takeover of a Japanese piston manufacturing plant in the spring of 2003 the Automotive sector strengthened its core capabilities for systems and modules "for every aspect of the engine." The acquisition marks a further milestone in the expansion of operations in the Asian economic region. The electrical fuel pump product group no longer fell within the defined core competencies and was sold as of January 1, 2003. This decision was based on the tendency among carmakers to give priority to suppliers of complete tank and fuel delivery systems (first tier) when awarding contracts in this segment.

At Aditron AG, a squeeze-out process was initiated, which with the entry of the stockholders' decision in the Commercial Register on June 24, 2003, resulted in the complete repurchase of outstanding shares held by minority stockholders. In order to revamp the Group's organizational structure, Aditron AG was merged with Rheinmetall AG retroactively as of January 1, 2003. As part of the fundamental future strategy of concentrating within the Rheinmetall Group on the two core activities with the highest sales, Automotive and Defence, the interest in the Preh Group was sold to a financial investor as of October 31, 2003.

The sale of the Jagenberg Group's mechanical engineering operations was completed during the year under review as planned. The EuroMarine Group, which had the status of a financial holding, with

Rheinmetall's rising from 50 to 100 percent at the start of 2003, disposed of all STN Atlas Marine Electronics GmbH's business activities as of October 31, 2003. The sale of the remaining part of EuroMarine with an annual sales volume of about €46 million is planned for 2004. The EuroMarine Group was included at equity for the months of January and February 2003 and for the rest of the year as a fully consolidated subsidiary.

Transparent shareholding and management structures have been created thanks to the sharp reduction in minority interests. In January 2003, the holding in Oerlikon Contraves AG was increased to 100 percent. In April 2003, Rheinmetall AG submitted a voluntary public offering for the free-floating stock of Kolbenschmidt Pierburg AG. Rheinmetall's stake in this subsidiary came to 95.5 percent as of December 31, 2003.

Progress in emission reduction: Pierburg's exhaust gas recirculation system meets the latest emission control standards

The situation of the Group

Sales trend shows organic growth of 4 percent

In fiscal 2003, the Rheinmetall Group generated sales of €4,248 million. This 7-percent fall compared with the previous year was exclusively attributable to changes in the consolidation group and to exchange rate effects. Adjusted for these effects, group sales climbed 4+ percent. Automotive and Defence, the two core sectors, together accounting for 82 percent, again contributed the lion's share of group sales.

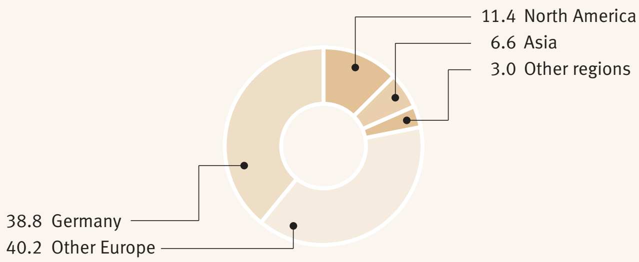
Sales by corporate sectors *€ million*

	2002	Share of total sales	**2003**	Share of total sales
Automotive	1,883	41%	1,884	44%
Defence	1,677	37%	1,605	38%
Electronics	802	18%	501	12%
Others/consolidation	209	4%	258	6%
Rheinmetall Group	4,571	100%	4,248	100%

During the period under review, the Automotive sector managed to raise its business volume slightly especially due to Aluminum Technology's upswing. Adjusted for currency effects and consolidation group changes, an organic growth of 4 percent was recorded, well above the production growth of 1.6 percent in the world's auto industry. Sales at Defence declined owing to the STN Atlas Elektronik split-up. Sales by the Naval Systems unit, which had been fully consolidated in the previous year, were included in the 2003 income statement only up to August 1, 2003. Taking into account all consolidation group changes, the Defence sector achieved organic growth of 5 percent, Land Systems, in particular, recording high sales gains. The shortfall in sales at Electronics was attributable to extensive divestments, starting with the sale of Heimann Systems in November 2002. The Euro-Marine Group, fully included in the consolidated financial statements under Others since March 1, 2003, outcompensated the sales lost after the disposal of Jagenberg.

Non-German sales in the Rheinmetall Group came to 61 percent of the total (down from 62 percent). Automotive's non-German business rose from the year-earlier 67 to 68 percent. In the Defence sector, sales to foreign customers likewise advanced, from 56 to 57 percent. According to regions, Rheinmetall's sales share in Europe and North America receded slightly while the sales volume in Asia increased.

Sales 2003 by region *in %*



Total net sales by the Rheinmetall Group: €4,248 million

Order situation affected by deconsolidation

Order intake declined in fiscal 2003 compared with the very high prior-year level by 15 percent to €4,128 million. The chief reasons for this fall were the changes in the consolidation group as well as the postponement of major contracts in the Defence sector. At €3,143 million, orders on hand as of December 31, 2003, were well below the previous year's. The Defence sector's order backlog contracted from €3,649 million to €2,748 million. Of this decline, €791 million was attributable to the order backlog held by the year-end divested Naval Systems unit. Among the orders on hand are some that will stretch over several years.

Earnings affected by one-time factors

Nonrecurring factors impacted again on the Rheinmetall Group's earnings in 2003. At €204 million, the Group's 2003 EBIT slid down far below the prior year's €392 million, which had also been boosted by the high gain of €246 million from the divestment of Heimann Systems. The Automotive sector ratcheted up its EBIT by 6 percent to €103 million while Defence, despite the deconsolidation of Naval Systems during the period, reported an EBIT of €69 million and thus roughly repeated the 2002 performance.

EBIT by corporate sectors *€ million*

	2002	**2003**
Automotive	97	103
Defence	72	69
Electronics	327	45
Others/consolidation	(104)	(13)
Rheinmetall Group	392	204

Like-for-like adjusted EBIT significantly above 2002's

In adjusted EBIT terms, Rheinmetall's performance improved from €213 million in 2002 to €223 million in the year under review. The disposal of equity interests produced on balance a net gain of €26 million: While particularly the divestment of STN Atlas Marine Electronics, the Preh Group and the Electric Fuel Pump unit was closed with net book gains, the sale and transfer of Jagenberg entailed a book loss. Realty transactions generated a €7 million income in 2003. Restructuring-related expenses totaled €52 million, including €14 million alone for Defence's Unterlüss location. The multiple changes in the consolidation group—inter alia resulting in the loss of profit contributions from Heimann Systems and Naval Systems—were outcompensated by the upgraded operating performance of Rheinmetall's mainstream business, Automotive and Defence. When additionally allowing for all consolidation group changes (by restating 2002 on the basis of the 2003 shareholdings), the like-for-like adjusted 2002 EBIT of €181 million was outnumbered by the same-portfolio EBIT 2003 by 20+ percent.

The situation of the Group

Like-for-like adjusted EBIT *€ million*	2002	**2003**
EBIT	392	204
Nonrecurring losses/gains from		
shareholdings	(219)	(26)
realty	5	(7)
restructuring	35	52
Adjusted EBIT	**213**	**223**
Consolidation group changes	32	--
Like-for-like adjusted EBIT	**181**	**223**

Net interest expense again downscaled

Thanks to the lower debts, radically downscaled in the past years, Rheinmetall's net interest expense decreased by another €18 million to a negative €84 million. The tax load ratio rose to slightly above the Group's normal level, due to the loss on the disposal of Jagenberg not being tax-deductible. The minority interests in net income dropped by €23 million to €5 million. This decline benefits all Rheinmetall stockholders and reflects the successful repurchase in 2003 of minority interests.

Adjusted EpS ramped up

↗ *page 12*

↗ *cf. Note (30) on page 92*

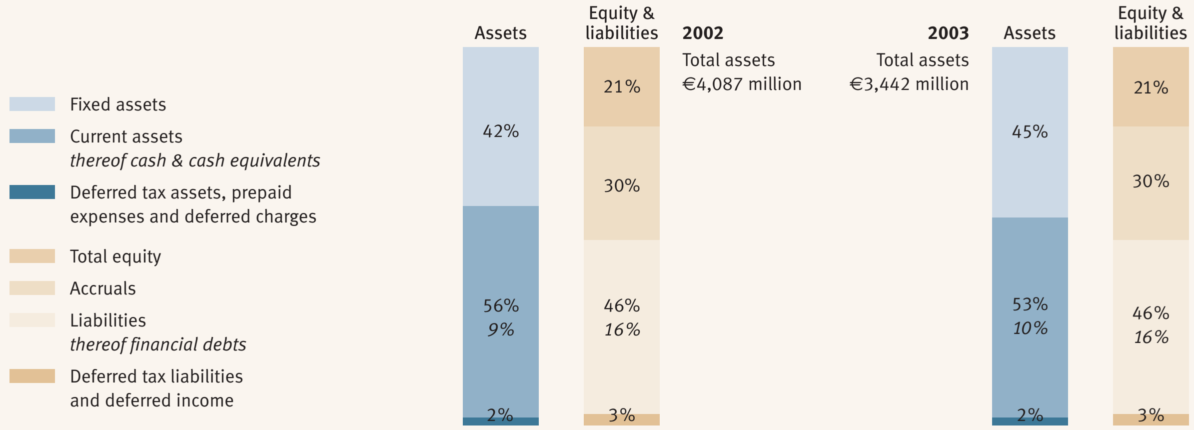
Earnings per preferred share (unadjusted for one-time factors and before goodwill amortization) receded from €7.95 to €2.62 while, in terms of adjusted earnings before goodwill amortization, they rose from €1.83 to €2.85 ↗. Adjusted EpS per preferred share is determined by deducting from the EBT which has been adjusted for nonrecurring income and expenses ↗ the 40 percent tax rate expected for the Group and adding back the goodwill amortization not included in untaxed reserves. This clearly improved performance is the outcome of the Clear Directions strategy, which centers on profitable core operations, downsizing debts and reducing minority interests in subsidiaries.

Group net income *€ million*	2002	**2003**
EBIT	**392**	**204**
Net interest expense	(102)	(84)
EBT	**290**	**120**
Income taxes	(16)	(52)
Group net income	**274**	**68**
Minority interests	(28)	(5)
Group earnings (after minority interests)	**246**	**63**

Asset and capital structure: debt downsizing continued

In fiscal 2003, the Rheinmetall Group's total assets shrank 16 percent to €3,442 million, largely due to sizable divestments, which appreciably reduced both fixed and current assets. Fixed assets diminished to €1,549 million, hence down by €183 million of which €133 million was caused by major changes in the consolidation group, the balance being attributable to lower capital expenditures. Current assets were slimmed down from €2,274 million to €1,815 million, the consolidation group changes accounting alone for €499 million of this decrease. The stockholders' equity inched up while total equity moved down from €869 million to €731 million, essentially as minority interests in subsidiaries were lessened. At 21 percent, the equity ratio remained virtually unchanged. Financial indebtedness continued to be downsized in 2003, from €668 million to €566 million. Deducting cash and cash equivalents brings net financial debt to €230 million (down from €301 million). Net leverage (as the ratio of net financial debt to equity) improved from 34.6 to 31.5 percent.

Asset and capital structure



Source and use of value added

In fiscal 2003, the value added by the Rheinmetall Group declined from the prior year's €1,907 million to €1,612 million. The Group's total operating performance fell 10 percent to €4,592 million, due to the lower sales as the consolidation group shrank, as well as to reduced other operating income. The input was down €134 million to €2,738 million. The cost of materials—at 74 percent accounting for the lion's share of total input—was ratcheted down by 3 percent to €2,014 million. Also down were the other operating expenses, amortization of intangibles and depreciation of tangible assets. Value added per capita (rounded) dipped from €69,000 to €64,000.

At 86 percent, the workforce benefited from most of the value added. Lenders/banks accounted for 6 percent, the Treasury's share quadrupled from 1 to 4 percent. The higher taxes (in comparison to 2002) were inter alia ascribable to the nondeductibility of the losses on the Jagenberg divestment. Stockholders received an unchanged 1 percent. The residual 3 percent of value added remained within the Rheinmetall Group.

Source and use of value added *€ million*

	2002		**2003**	
Source				
Group's total operating performance	5,088		4,592	
Input	2,872		2,738	
Amortization/depreciation	309		242	
Value added	1,907		1,612	
Use		*in %*		*in %*
Employees	1,486	78	1,380	86
Treasury	27	1	65	4
Lenders (banks)	120	6	99	6
Stockholders	24	1	24	1
Rheinmetall	250	14	44	3
Value added	1,907	100	1,612	100

The situation of the Group

Capital expenditures in 2003 at €203 million

Rheinmetall's additions to tangible and intangible assets (excluding goodwill) amounted to €203 million. The 18-percent reduction resulted from both divestments and Automotive's scheduled expenditure shrinkage. As a percentage of sales, capital expenditures dropped from 5.4 to 4.8 percent within the Group. Amortization and depreciation (excluding goodwill) came to €211 million, exceeding outlays by €8 million.

Capital expenditures by corporate sectors *€ million*

	2002	2003
Automotive	144	127
Defence	48	46
Electronics	41	27
Others	15	3
Rheinmetall Group	248	203

Automotive: spending to improve ROCE

Automotive spent €127 million (down from €144 million). The additions to tangible assets include those of a Japanese pistons builder acquired under an asset deal; adjusted for this, the year's amount was €117 million, equivalent to 6.2 percent (down from 7.7 percent) of sales. The again improved expenditure deployment in 2003 is the outcome of the strictly enacted ROCE action package introduced the year before. Included among the year's most important measures for again downscaling expenditures as a percentage of sales were the outsourcing of manufacturing input not inherent to Kolbenschmidt Pierburg's core capabilities, increased interlocational coordination of idle capacities and production equipment, a closer focus on lean production potentials, and less reliance on work performed by specialty machinery. Most of the money went toward setting up and expanding capacities for new customer projects plus replacement/rationalization outlays at the Pierburg and Pistons divisions. Some 51 percent of the total was spent in Germany, 49 percent abroad, chiefly Europe. Depreciation by Automotive in fiscal 2003 added up to €132 million (slightly down from €134 million). Adjusted for the acquisition-related tangible-asset additions, capital expenditures during the past fiscal period at €117 million were some 11 percent short of depreciation. The year before expenditures had topped depreciation by around 8 percent.

Defence outlays for IT structure

Defence spent €46 million (down from €48 million), again equivalent to 2.9 percent of sales. Divisional spending varied by emphasis: Land Systems continued to implement its pan-locational Product Data Management system designed to coordinate for optimum efficiency development and design efforts across all locations. At Air Defence Systems and Weapon & Ammunition, spending prioritized the necessary replacement of available plant and equipment. Defence Electronics focused on its IT infrastructure. The splitting of Bremen-based STN Atlas Elektronik GmbH entailed expenditures for factory and office equipment. Defence's total spending in Germany accounted for 63 percent (down from 65 percent) and contrasted with depreciation of €52 million.

The world's most frequently used reconnaissance vehicle of its kind: the NBC Fuchs

The situation of the Group

Altogether €183 million on R&D

Technological progress is a precondition for Rheinmetall to offer its customers the best possible product solutions. Assimilated knowledge and expertise plus longstanding experience combined with the latest R&D techniques to deliver innovative products with evident customer benefits. In 2003, altogether €183 million went toward R&D for new products and technologies (down by 11 percent due to the smaller consolidation group). A total of 2,400 persons (down from 3,300) were employed at year-end 2003 in R&D at Rheinmetall.

R&D expenditures *€ million*

	2002	% of sales	**2003**	% of sales
Automotive	86	4.5	81	4.3
Defence	66	3.9	60	3.7
Electronics	48	6.0	38	7.6
Others	6	3.0	4	1.6
Rheinmetall Group	206	4.5	183	4.3

Automotive: debut of an electric coolant pump

www.rheinmetall.com/ppit.php

Once again, the Automotive sector accounted for the lion's share of €81 million. At Pierburg (Air Supply & Pumps), most of the R&D activities centered on performance enhancement projects plus emission and weight reduction. Many of these related to electronically controlled products which, in contrast to conventional mechanical components, lead to lower fuel consumption due to variable operation depending on operating conditions. Among the biggest individual projects were two magnesium intake manifolds remarkable for their significant weight advantages over conventional gray cast iron or aluminum, plus the debut of an electrical coolant pump due to enter series production in fiscal 2004.

For years now, enhancing power density and downscaling consumption and emissions have been the factors driving the development of new engine components at the Pistons division. In the case of gasoline engines, this mainly entails performance upgrading through direct injection and/or variable valve timing. Within such environments, the pistons are required to combine maximum strength with reduced mass. LiteKS is a casting technique that addresses these demands by reducing the piston skirt mass. Due to the further increase in power density, the pistons on the new car turbo diesel engines are only conceivable with integrated coolant passages. Kolbenschmidt Pierburg's GalleriKS technology inserts the coolant passage into the ring carrier for a further reduction in the critical temperature at the top piston ring groove. Improved materials compatible with maximum thermal and mechanical loads in car and commercial vehicle engines are now ripe for production. For large-engine pistons, maximum strength single and multi-part steel pistons have been developed and delivered to a number of customers for field testing.

Market demand for lead-free materials was the dominant factor at R&D by the Plain Bearings division. Efforts were again stepped up to develop plain bearings capable of addressing the growing insistence on eco-friendly materials.

Aluminum Technology's R&D again focused on achieving consistent and reproducible casting and machining processes, materials development including local material reinforcements, and extending the scope of downstream machining.

Defence: New infantry fighting vehicle under development

In the Defence sector, development of the new Puma infantry fighting vehicle was a focal point of attention. The Puma can accommodate a nine-member crew, is provided with highly effective modular armor and meets the requirement of rapid deployment. Together with a Swiss partner, the 6x6 multipurpose Duro 3 vehicle was developed, which besides having a generous payload capacity, offers high protection against mines and ballistic threats. Another key focus of activity was the further development of a component which can be integrated into NBC vehicles and for the first time enables on-board reconnaissance and analysis of biological warfare agents.

The Air Defence Systems unit completed the development of the 35-mm revolver gun. Its high rate of fire, automatic fire control unit and use of Ahead ammunition enable small aerial targets to be engaged more effectively. Development work continued on the highly mobile air defence system Spaag (Self-propelled anti-aircraft gun) and the Millennium naval gun system. Improvements were made to the Skyguard III air defence system, the highly sensitive 3D-X-Tar radar and the battle management system, which networks hitherto autonomously deployed air defence systems for improved air space monitoring and weapon deployment coordination.

www.rheinmetall-detec.com/nlw.php

Weapon & Ammunition's R&D activities centered on the 120-mm HE rounds program and on modifying the Leopard 2 weapon system to accommodate this new shell. On behalf of the Federal Government, work was conducted on developing laser and microwave weapons. The latter are to be used in the medium to long term chiefly against targets with a high electronic content. Using directed electromagnetic energy, these weapons are capable of putting electronic components out of action either temporarily or permanently without causing physical destruction. Additionally, systems for vehicle, personnel and area protection were further improved. They operate by directing special particles at the sensors of enemy weapons and creating decoys capable of deflecting incoming missiles and sea skimmers from their intended targets.

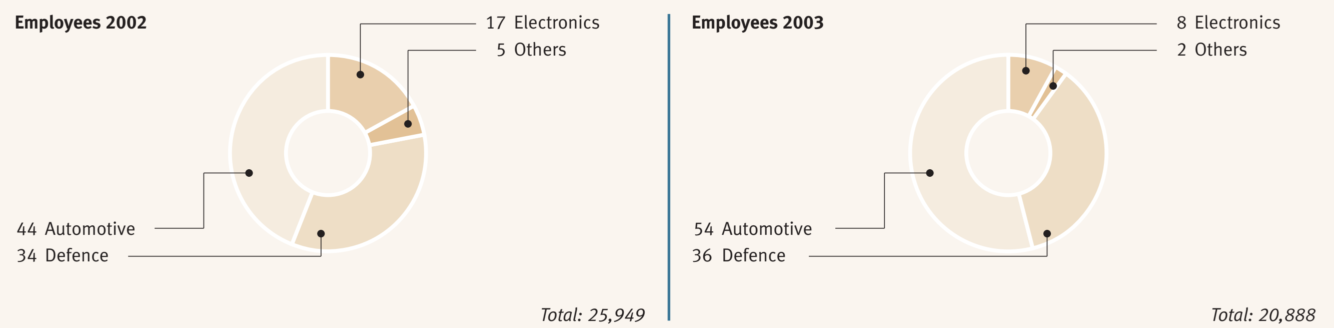
Defence Electronics demonstrated using a prototype the improved efficiency of the Seoss electronic periscope. This vehicle-mounted reconnaissance component enables moving targets to be detected and engaged, even when traveling at high speeds. An essential visualization component is the Saphir, a thermal imaging device whose development was successfully completed during the period under review. This latter sets new standards in terms of thermal resolution. At Aviation Systems, the capabilities of the Taifun attack drone were further developed and at Land Systems & Combat Simulation, a three-way laser simulator underwent additional improvement. Furthermore, multiple-application modules for constructing advanced flight simulators were successfully developed and used for the first time in Tiger and Eurofighter simulators.

Sharp drop in headcount following divestments

The Rheinmetall Group's companies operate in fiercely competitive and highly dynamic markets requiring a high degree of special expertise. Experienced executives, highly qualified experts, practice-oriented specialists and highly motivated junior managers identify with the company's aims, working across functional, divisional and national boundaries.

At the end of fiscal 2003, the Rheinmetall Group employed a worldwide workforce of 20,888, which was 5,061 people fewer than in the prior year. This reduction is chiefly due to the divestments in the year under review. The internationalization course consistently pursued by the Rheinmetall Group is reflected in the following figures: as of December 31, 2003, the number of people employed outside of Germany was 8,517 or 41 percent of the total headcount, up from the year-earlier 38 percent.

Employees by corporate sectors *in %*



The situation of the Group

Precision manufacturing:
the KS Pistons division meets the high standards of quality expected by international carmakers

Personnel expenses per capita inched up to €53,000 (rounded). This approximately 2-percent increase is mainly attributable to collectively negotiated pay rises.

Personnel expenses per capita *€ '000*	2002	**2003**
Personnel expenses per capita	52.2	53.1

With almost unchanged sales over 2003, sales per capita showed a 2-percent rise, which again underlines the Group's high productivity.

Sales per capita *€ '000*	2002	**2003**
Sales per capita	164.8	168.6

Competent and wide-ranging training which takes new developments in the labor market into account continues to enjoy high priority within the Rheinmetall Group. As in the preceding year, apprentices accounted for 5 percent of the workforce.

Apart from conventional and up-to-date instruments of personnel recruitment, in seeking to attract well-trained experts and executives the Rheinmetall Group relies on the targeted expansion of existing cooperation with polytechnics, universities, and research institutions. At key recruiting events and graduates conferences Group companies present themselves as an attractive employer, establishing contacts with promising young executives. The Internet is being used increasingly as a forum for establishing contact. The newly designed job applications portal offers a comprehensive overview of the career options within the Rheinmetall Group, making it possible to apply online ↗. Such applications can be passed on to the relevant departments within the Group promptly and examined with a view to possible recruitment. This streamlines the application process in the interests of both applicants and Rheinmetall.

↗ *www.rheinmetall.com/jobs.php*

Successful HR development programs

Personal and specialized qualifications, interlinked thinking and leadership qualities are becoming ever more important. The competitive pressure emanating from international markets requires a constant willingness to learn. The knowledge, skills and competence of Rheinmetall employees determine together with the existing information and corporate culture how the challenges and changes to be expected are overcome and whether the decisions made today will lead to corporate success tomorrow.

Consequently, we offer employees the opportunity to attend demanding external seminars and advanced training courses. Internal skills-upgrading programs which are tailored to corporate needs were responsibly conducted by the Rheinmetall Academy. The focus is on the subject areas of strategy, leadership, project expertise and globalization. A forum event as part of the Benchmarking series was devoted to best practice within the Group, enabling executives to learn from one another. A newly launched 15-month Young Manager Program prepares junior executives for their future managerial roles in a well-targeted manner. PC-supported learning methods are currently in the trial phase and expected to complement conventional training courses increasingly in the years ahead.

Rheinmetall relies on its ability to spot early on, and make the most of, the individual skills, talents and potentials of its employees. A working group has developed through systematic potential analysis a tool which objectivates the careful identification of exist-

The situation of the Group

ing management, expert and junior management potential within the Group while harmonizing this process and making it more transparent. Key areas of development aimed at deepening and extending existing strengths are defined and professional, multi-stage training courses offered. High-potentials can be retained by the Group through promising career prospects and scope for success. The results of the potentials analysis also provide information on sound staffing and succession planning, and demonstrate the need for area-specific measures such as advanced skills-enhancing schemes and changed tasks.

Profit-related and meritocratic pay structures

The management culture in the Rheinmetall Group combines strength in terms of the strategy being pursued and clear performance expectations with tangible orientation toward implementation and results. Attractive, fair market conditions of employment and consistent value-enhancement compensation and incentive systems promote motivation and results. Executive and management board members as well as other senior executives receive a variable pay component which is linked to corporate success and the achievement of agreed targets. This meritocratic compensation system for managerial staff creates an individual incentive to surpass set goals as much as possible besides allowing executives to share in the risks and rewards of their business. In addition, an incentive program has been introduced which is geared to the absolute annual increase in the Group's shareholder value. As part of the management by objectives (MBO) program, employees below executive level are also being managed increasingly according to agreed goals. A groupwide works agreement envisages that all employees will be included in the MBO scheme by 2005.

Pension plans—an integral part of personnel policy

In the wake of the pension reform which took effect in Germany in 2002, employee pension schemes are gaining in importance. The Rheinmetall Group supports its employees in planning and implementing a plan which supplements statutory pension insurance, thus increasing financial security in old age. This forward-pointing pension scheme, which applies to all Rheinmetall's domestic plants, consists of three components: a reliable basic plan, an intermediate profit-related plan linked to the enhancement of shareholder value and an employee-funded supplementary plan, which enables various forms of payment conversion (deferred compensation, direct insurance, partly employee-/partly state-funded pension based on the Riester model).

Information and know-how transfer

The relevant knowledge is being continuously revised and updated through the growing flood of new information displacing existing. Against the background of a rapidly changing business environment, adjusted performance targets and strategic initiatives have to be implemented increasingly quickly. The transfer of information and knowledge within the Rheinmetall Group as well as the establishment of virtual team rooms and project and knowledge databases are being advanced by supplementing the existing intranet with the groupwide, software-supported gate2rheinmetall communications portal. This tool for the systematic structuring of the knowledge and expertise available within the Group builds on existing processes, takes account of tried-and-tested practices and is supported by an IT infrastructure which links and reflects existing and yet-to-be-created modules of knowledge management.

Rewarding bright ideas

The knowledge, ability, experience and creativity of the workforce play an important part in boosting productivity and economic efficiency. Rheinmetall's corporate suggestion scheme serves as an efficient tool in promoting workforce commitment. During the past fiscal year, the 5,100 proposals submitted by employees once again helped the Rheinmetall Group's companies to advance their products and work flows and thus operate with enhanced efficiency, safety and environmental compatibility.

Responsibility for humankind and the environment

The business activities of the Rheinmetall Group are characterized by a sense of overall responsibility for humankind and the environment. The economical use of raw materials and energy therefore forms a central entrepreneurial basis for the operations of group companies, as does the responsible handling of residues and emissions. It is crucially important in this regard that environmental protection in the Rheinmetall companies is pursued not as a downstream, purely requirement-oriented task but also—in accord with an holistic understanding—as an integral part of the management system. Employees' sense of responsibility for the environment is therefore promoted at all levels of the value chain. For Rheinmetall environmentally compatible stewardship starts with the inception of new products and continues at all stages of series manufacture.

Effective, efficient environmental management results not least from the way that Rheinmetall companies define themselves in all their operations through top engineering performance while striving universally for market supremacy. The standards set for all internal corporate processes are correspondingly high.

Moreover, the Automotive sector as a key partner of the automobile industry with numerous products is making a significant contribution to reducing pollutant emissions and energy consumption—a market positioning which also places an obligation on the sector's internal procedures. In order to safeguard the environmental objectives set, exacting environmental management systems have been implemented in both the domestic and foreign production companies of Kolbenschmidt Pierburg AG and approved in accordance with the internationally recognized ISO 14001. This procedure is due to be completed in 2004. In addition, training courses and the regular provision of information have helped to develop a positive awareness of environmental issues on a broad scale within the companies.

The continuous further improvement of environmental and safety management is also defined as a permanent corporate goal at Rheinmetall DeTec AG. In compliance with the specific requirements of its fields of work, all the main production sites belonging to the Rheinmetall DeTec Group have been approved under the internationally valid quality management standard ISO 9001. Additionally, Oerlikon Contraves AG, the two production plants belonging to the Nitrochemie Group and Pyrotechnik Silberhütte GmbH hold the environmental approval under ISO 14001.

Numerous examples from the Rheinmetall Group demonstrate that economic and environmental activities are not conflicting aims in a progressively run company. Environmental programs have lowered operating energy costs in all sectors, thus making an important contribution to increased competitiveness. For example, the energy consumed by Oerlikon Contraves AG at its Zurich plant has dropped by almost 20 percent since the initial official approval in 1998. This is equivalent to annual savings of more than €0.3 million. Together with the changeover to district heating, CO_2 emissions have also been cut by more than 60 percent.

Rheinmetall AG

Rheinmetall AG performing strategic holding functions

The functions of Rheinmetall AG are to manage the Group as such, as well as the portfolio of shareholdings and the realty in Unterlüss/Neulüss. Rheinmetall AG's role is that of a strategic holding company subsuming the corporate departments of Legal Affairs, Controlling, Finance, Human Resources, and Communications. As of December 31, 2003, its staff totaled 77 (down from 78), the 2003 headcount averaging 82.

Through intermediate holding companies, Rheinmetall AG is affiliated with the subgroup parents of Automotive and Defence. As management holding company, Rheinmetall AG continued in 2003 the strategic realignment of the Rheinmetall Group by concentrating on only two mainstream business segments, Automotive and Defence, and selectively shedding and acquiring companies. In fiscal 2003, Rheinmetall Elektronik GmbH and then Aditron AG as intermediate holding companies were merged into Rheinmetall AG.

Unlike the consolidated financial statements, Rheinmetall AG's separate financial statements continue to be prepared in accordance with HGB regulations.

Rheinmetall AG's earnings in 2003, too, basically consisted of financial income (from investments and interest) as well as service and management fees apportioned to group companies, less the related personnel and impersonal expenses. The investment income of €143 million (up from a red €7 million) includes €161 million a gain from the merger with Aditron AG. Net interest expense contracted from a negative €19 million to a negative €15 million. The net financial result turned around, soaring from a negative €26 million the year before to €128 million in 2003.

Other operating income of €52 million, other operating expenses of €31 million, personnel expenses of €27 million and amortization/depreciation of intangible and tangible assets of €2 million combined (of course, including the net financial result) to produce an EBT of €120 million, up by €112 million from €8 million. The other operating income mainly includes the book gain from the disposal of an investee, as well as rental income from properties leased to Rheinmetall DeTec AG, plus income from intercompany allocations. Together with income tax expenses of €8 million (up from €2 million), this yielded a net income of €112 million (up from €6 million). After transferring €46 million to the reserves retained from earnings, Rheinmetall AG's net earnings came to €66 million.

Rheinmetall AG's results of operations are directly related to the business trend of its corporate sectors and its service companies.

Designed for international assignments: the new armored multipurpose Duro 3 offers its occupants a scale of protection so far unachieved in this category of vehicle

The corporate sectors: Automotive

Reduced weight: Magnesium intake manifolds from Pierburg are employed in large-volume medium- and premium-class engines

Amplified presence in Asia

Pierburg GmbH sold its electric fuel pump unit as of January 1, 2003, a step in the direction of consistent focus on core business and in line with the auto industry's preference to place fuel pump orders with first-tier suppliers of tank and fuel delivery systems. The sector's presence in the fast-growing Asian market was amplified during the period under review. As of February 4, 2003, KS Kolbenschmidt GmbH, the parent company of the Pistons division, acquired through its subsidiary Kolbenschmidt K.K., Japan, the pistons business of Microtechno Corp., Japan, from Mazda Motor Corp., Japan. The transfer took the form of an asset deal. In Great Britain, the Motor Service division wound up its KS Winston Ltd. at the start of March 2003, such business in future being channeled through a distributor directly via MSI Motor Service International GmbH.

In fiscal 2003, the Automotive sector generated sales of €1,884 million, just above the prior-year €1,883 million. The sales generated in the past fiscal year had been affected by a number of special factors, adjusted for which Automotive achieved a 4+ percent growth over 2002. These nonrecurrent factors included translation–related exchange rate effects, especially resulting from the euro's changed currency parities in relation to the US dollar and the Brazilian real, as well as structural effects from the sale of the electric fuel pump unit and the acquisition of the Japanese Microtechno Corporation's piston business. Once again customers abroad accounted for about two-thirds of total sales. The sales breakdown by region shows for Europe including Germany a 76-percent share (virtually unchanged). Among overseas markets, North America remained the key region in 2003, with a 16-percent share of sales. This represented a slight fall on the prior year mainly owing to the weak US dollar, although in local currency US business expanded

Automotive indicators *€ million*

Kolbenschmidt Pierburg AG	2001	2002	**2003**
Net sales	1,826	1,883	1,884
Order intake	1,843	1,917	1,860
Order backlog (Dec. 31)	305	339	314
EBIT	91	97	103
EBT	50	60	72
Employees (Dec. 31)	11,662	11,535	11,316
Average capital employed	897	827	748
EBIT margin *in %*	5.0	5.2	5.5
ROCE *in %*	10.1	11.8	13.8

The corporate sectors: Automotive

by about 13 percent. The remaining world markets accounted for 8 percent of group sales, with Asia's higher sales share based on the purchase of a Japanese piston manufacturer completed in 2003. Kolbenschmidt Pierburg's EBIT for fiscal 2003 totaled €103 million, up from €97 million.

Pierburg division burgeoning

Pierburg's sales dipped by 0.7 percent to €878 million, which due to the sale of the electric fuel pump unit coupled with unfavorable translation-related currency effects failed to reflect this division's commendable performance. Adjusted for these factors, Pierburg's sales climbed. The Air Supply unit, the prime source of sales growth in the past, could not fully compensate for the cancellation of a series production project brought about by the OEM's decision to phase out an engine. By contrast, emission control products sold appreciably better, especially thanks to the brisk demand for exhaust gas recirculation valves. Pumps failed to match its prior-year sales level due to the disposal of the electric fuel pump unit but presided over very encouraging electric water pump business. Pierburg's EBIT fell by €7 million to €58 million. Adjusted for the sale of the electric fuel pump unit and some real property in Italy during the past fiscal year, the sale of the stake in Preh GmbH & Co. KG in the previous year and provisions for restructuring, the good prior-year profit was topped, however. The Spanish subsidiary again registered very pleasing profits, whereas the Italian subsidiary's marked improvement on the previous year was concealed by expenditure for more extensive restructuring measures, resulting in a loss for fiscal 2003. The company in the North American market managed to make a higher contribution to profit than 2002 despite a drop in sales.

The Pistons division generated sales of €594 million in the past fiscal year, falling just short of the prior-year €596 million because of changed currency parities. The North and South American companies in particular boosted sales, often considerably, in local currency. When adjusted for structural and exchange rate effects, sales by the Japanese pistons operations (acquired in 2003) showed an uptrend. KS Pistons' EBIT increased by €10 million to €38 million. The evident improvement in earnings is chiefly due to the US restructuring programs provided for in the year-earlier accounts. Even after eliminating the currency translation effects and despite the provisions for restructuring one of the German plants and the profit turned in by the Japanese pistons operations (initially consolidated in 2003), the outcome is a growth in net operating result. Among the reasons for this progress are the successful restructuring measures in the North American companies as well as the again solid profit contribution from the Brazilian subsidiary. The French investee largely made good the sales-related profit shortfall in fiscal 2003 with cost savings and increased productivity. The Czech subsidiary succeeded in compensating for declining business volume by remixing to its own advantage the product lineup and thus posting a favorable profit at the year-earlier level.

The Plain Bearings division raised sales slightly by €1 million to €147 million, with notable gains registered in high-duty plain bearings and connecting rod bushings business. At €9 million, the division's EBIT was slightly below the 2002 level despite operative improvements. The German management company's profit again matched the favorable prior-year level, with the Brazilian subsidiary achieving an improved profit contribution. In contrast, the US subsidiary's still red EBIT eroded the division's earnings. Risk management measures taken by the company outweighed the progress achieved through its operations.

Aluminum Technology's sales and earnings up

In the Aluminum Technology division, product start-ups of innovative high-end engine blocks by premium-segment manufacturers in Germany, especially in the low-pressure casting sector, caused sales to climb 7.4 percent to €160 million. Compared with 2002, the Aluminum Technology division slashed its loss by €10 million to (an albeit red) €3 million, especially thanks to the substantial advances in productivity and quality achieved in low-pressure castings production.

The Motor Service division was not able to evade the weak demand in individual aftermarkets, its sales of €139 million representing a dip of €7 million on fiscal 2002. At €16 million, the division's EBIT was slightly above the prior-year level, however. Measures aimed at reducing costs further—especially at the German company—and a streamlined product portfolio more than compensated for the adverse effects from declining sales.

OEM-quality spare parts: MSI supplies auto workshops and repair facilities worldwide

The corporate sectors: Defence

Top-class technology: close-range air defence systems from Oerlikon Contraves

Major structural changes after Naval Systems spin-off

The main structural change of fiscal 2003 concerned the Naval Systems and Central Production units and some of the staff functions at STN Atlas Elektronik GmbH, which were split off as of July 31, 2003, and transferred to STN Atlas Elektronik GmbH's former co-shareholder, BAE Systems Deutschland GmbH. The now wholly-owned subsidiary STN Atlas Elektronik GmbH has been operating as Rheinmetall Defence Electronics GmbH since August 13, 2003, comprising Land & Aviation Systems as well as Simulation Systems. The transferred units were included in Rheinmetall DeTec AG's consolidated income statement up to deconsolidation date. Moreover, Rheinmetall DeTec AG increased its holding in Oerlikon Contraves AG, Zurich, on January 2, 2003, by 19.5 percent to 100 percent. In the Weapon & Ammunition division, the subsidiaries Nico Pyrotechnik Hanns-Jürgen Diederichs GmbH & Co. KG, Nico Feuerwerk GmbH and Pyrotechnik Silberhütte GmbH were fully consolidated by Rheinmetall DeTec AG for the first time as of July 1, 2003. Netherlands-based Eurometaal N.V. was, as decided in 2002, finally closed down in fiscal 2003. As a response to significant changes in the German armed forces' procurement planning, which resulted in drastic cuts in the development and production of large-caliber ammunition, Rheinmetall W&M GmbH had to undergo surgery aimed at adjusting capacity and reducing the workforce, especially at the Unterlüss plant.

Net sales by Defence reached €1,605 million, down by 4 percent. The shortfall on the previous year was chiefly ascribable to the deconsolidation of the Naval Systems and Central Production units belonging to the former STN Atlas Elektronik GmbH, Bremen. Adjusted for all consolidation group changes, sales in fiscal 2003 were about 5 percent higher than the year before. Accounting for 57 percent, sales to customers outside of Germany proved predominant, rising from the year-earlier 56 percent and reflecting Defence's continued efforts to expand its international activities. The chief sales region remained Europe (excluding Germany), which accounted for 39.5 percent of sales in 2003. The sector's order intake totaled €1,473 million (down from €1,861 million). This lower level of incoming business was especially due to consolidation group changes and a smaller number of megaprojects. In fiscal 2003, Defence's EBIT fell from the prior-year €72 million to €69 million, a commendable result given the major consolidation group changes and the heavy restructuring costs, especially due to the shrinkage at Rheinmetall W&M.

Defence indicators *€ million*

Rheinmetall DeTec AG	2001	2002	**2003**
Net sales	1,614	1,677	1,605
Order intake	1,999	1,861	1,473
Order backlog (Dec. 31)	3,462	3,649	2,748
EBIT	61	72	69
EBT	36	50	46
Employees (Dec. 31)	9,019	8,828	7,435
Average capital employed	629	585	528
EBIT margin *in %*	3.8	4.3	4.3
ROCE *in %*	9.7	12.3	13.0

The corporate sectors: Defence

Weapon & Ammunition stepping up sales

www.rheinmetall-detec.com/hpm.php

In the period under review, the Weapon & Ammunition division generated sales of €567 million (up from €551 million). Rheinmetall W&M GmbH's deliveries of LKE II tank ammunition and SMArt sensor-fuse ammunition again constituted the bulk of sales. Shipments of the BK 27 board cannon for the Eurofighter and the Nitrochemie Group's artillery charges also made a sizable impact on sales. With incoming orders amounting to €480 million (down from €518 million), the division contributed the lion's share of the Defence sector's order intake. Most notable among the orders successfully booked were the contracts for the Leopard 2 battle tank's 120-mm weapon system from Greece and for the supply of 225,000 rounds of 27-mm ammunition for the 83 series production light naval guns commissioned in the preceding year and bound for the German navy. In the market for nonlethal impact agents, whose importance is set to accelerate in future, various orders were secured for the development of medium-energy laser and high-performance microwave products. Weapon & Ammunition's EBIT of €37 million was €4 million up over 2002's.

In 2003, the Defence Electronics division generated sales of €406 million, which, owing to the splitting of STN Atlas Elektronik GmbH, fell some 29 percent short of the year-earlier €573 million. The shipment of further combat systems based on a multi-year contract for the Spanish version of the Leopard 2 battle tank and of LeFlaSys light air defence systems to the German armed forces formed the mainstay of sales in 2003. Other sources were the services arising from a development contract for simulation-supported training facilities for crews on the new Tiger combat helicopter and a contract from Germany for the series production of unmanned air vehicles for target detection. The division booked incoming orders worth €419 million, which, because of the restructuring of STN Atlas Elektronik GmbH, were below the year-earlier €521 million. During the period under review, the fire command system for the Leopard 2 battle tank to be delivered to Greece and the contract to equip the Finnish armed forces with the Spike anti-tank system were notable new business successes. Defence Electronics' EBIT reached €12 million, which due to the STN Atlas Elektronik GmbH costs as well as the only prorated profit of the Naval Systems and Central Production units, fell well short of the prior-year €29 million.

The MLG 27 light naval gun: provides self-protection for battle ships and smallish floating units

Land Systems multiplying its EBIT

www.rheinmetall-detec.com/mms.php

In the period under review, Land Systems generated sales of €331 million (up from €248 million). This approximately 34-percent rise was chiefly attributable to the successful booking of major contracts in 2002. The prime sources of sales were recovery vehicles for the Swedish army, the production of 2000 tank howitzer chassis and the equipping of the Marder infantry fighting vehicle with an improved mine protection system. The division received orders worth €323 million (down from €480 million) in 2003, most notably for the production of chassis for the tank howitzers ordered from Italy and for the recovery tank 3 for the Greek army. In addition, a contract was awarded for conducting an efficiency and protection upgrade program on the German armed forces' Fuchs transport vehicle. The successful restructuring drive at Land Systems resulted in an EBIT of €13 million, far above the preceding year's €3 million.

The Air Defence Systems division's sales in 2003 came to €332 million, thus matching the prior-year level, significant sources of sales being the Skyguard and Skyshield air defence systems. Fiscal 2003 saw the shipment for the first time of a complete fire unit for the new-generation Skyshield system. Apart from air defence systems business, the information and reconnaissance management unit also made a significant contribution to sales. Order intake amounted to €287 million (down from €390 million) and was achieved despite the postponement of major contracts from the Middle East in the wake of the Iraq crisis. The chief contracts secured in 2003 were for a combat upgraded version of the 35-mm Skyguard systems from a NATO state and for the shipment of Sparrow missile launchers to an Asian country. An Eastern European country placed an order for Gun Star components packages including a stock of replacement parts. Air Defence Systems' EBIT reached €14 million, down from €18 million in 2002.

Others

Electronics: Hirschmann and Preh

Following the sale of the Heimann Systems division (security) in 2002, the year under review in the Electronics sector (Aditron Group) was marked by major ownership changes, which resulted chiefly from the strategic decision to shed this sector. At the same time, the Electronics operating companies, Hirschmann and Preh, further improved their economic efficiency during fiscal 2003.

Electronics' close focus on its automobile electronics business (accounting for over 50 percent) again paid off in 2003. According to industry insiders, by 2010 electronics will account for 35 percent (presently around 22 percent) of the value of a car. In contrast, with industry still keeping its purses tight, the sector's industrial electronics business again receded slightly. Likewise, the recession in the construction machinery industry hampered sales of electronics for such equipment, albeit appropriate restructuring programs succeeded in comfortably absorbing such burdens.

Prestigious contracts, such as the implementation of a universal Industrial Ethernet network by Hirschmann in the production of the new VW Golf at Wolfsburg or Preh's air-conditioning control panel for the newest BMW 5-series, demonstrate that the Aditron companies hold strong competitive positions in their niche markets.

During the year under review, the Electronics sector's sales reached €501 million, down from the prior-year €802 million, this fall being solely attributable to the changes in the consolidation group. EBIT slumped from the year-earlier €327 million to €45 million in 2003, especially due to the one-off effects of Heimann Systems GmbH's disposal.

On March 7, 2003, Rheinmetall AG announced its intention to repurchase the free-floating shares in Aditron AG by squeezing out and paying off the minority stockholders. With the entry in the commercial register of the resolution adopted at the Aditron stockholders' meeting on May 15, 2003, the shares held by minority stockholders were transferred to Rheinmetall AG on June 24, 2003, in return for cash payment of €26.50 per no-par share. On the same day, Aditron stock was delisted on the Frankfurt/Main and Stuttgart stock exchanges. The Listing Boards of the Frankfurt and Baden-Württemberg stock exchanges revoked the relevant admissions in July 2003. Then, on October 15, 2003, Aditron AG was merged into Rheinmetall AG.

In order to streamline group structures and further enhance efficiency, Hirschmann Electronics GmbH & Co. KG absorbed its affiliate, PAT GmbH, in June 2003. The crucial reason for PAT's integration into the Hirschmann Group was especially the potential for synergies between PAT's construction machinery electronics unit and Hirschmann's Automation and Network Solutions product group. By contrast, PAT's transport telematics unit was sold to International Road Dynamics Inc., so that PAT GmbH within the Hirschmann Group with its Electronic Control Systems unit now concentrates exclusively on systems for load weighing and load moment limitation.

As part of a targeted divestment process, Rheinmetall AG sold its interest in Preh-Werke GmbH & Co. KG to Deutsche Beteiligungs AG in early October 2003, the transaction being closed as of November 1, 2003. This was preceded by the sale of Hirschmann Austria GmbH, a wholly-owned subsidiary of the Hirschmann Electronics Group, to Vorarlberger Privatstiftungen as of June 30, 2003. In February 2004, the divestment process was completed with the sale of Hirschmann, Neckartenzlingen. This transaction is expected to be formally closed by the end of March 2004.

EuroMarine Group

With effect as of November 1, 2003, the operations of STN Atlas Marine Electronics GmbH (SAM) were sold to EquiVest, a private equity investor. EuroMarine Electronics GmbH (EMG) now comprises EuroCom Industries A/S (ECI) based in Ålborg, Denmark. Previously included at equity, the EuroMarine Group was now fully consolidated as from March 2003.

EMG's encouraging performance again continued during the year under review. In its ten months of 2003, EMG generated sales of €217 million. Within a hostile market environment, the still remaining subsidiary ECI generated for the period March through December sales of €40 million. The Euro Marine Group's EBIT in 2003 was shaped by operational improvements in the companies and by the cash inflow from the SAM Group's disposal. Including these latter, EMG achieved an EBIT of €42 million.

Jagenberg Group

With the sale of Jagenberg AG including the only remaining operating company, Kampf GmbH & Co. Maschinenfabrik, the Rheinmetall Group completed the divestment of this business, marking its withdrawal from the mechanical engineering sector. Rheinmetall's majority stake of 93.7 percent was sold in full to Krefeld-based Kleinewefers Verwaltungs-GmbH as of July 31, 2003. Beforehand, Jagenberg AG had disposed of the operations of Lemo Maschinenbau GmbH based in Niederkassel-Mondorf as of June 30, 2003. At the start of the year, with effect as of January 31, 2003, the operations of Jagenberg Diana GmbH and Woschnik + Partner Maschinenbau GmbH as well as all of the shares in Jagenberg Slovensko sprl. s r.o. were sold to Heidelberg Erwerbs- und Verwaltungs GmbH, a subsidiary of Heidelberger Druckmaschinen AG.

During the past year, the Group's sales reached €64 million (down from €212 million), with order intake totaling €71 million (down from €230 million). Jagenberg's EBIT came to a negative €31 million (up from an equally red €15 million). The EBIT of fiscal 2003 also contained all the losses from the disposal of the Jagenberg companies.

Rheinmetall Service GmbH

Rheinmetall Service GmbH (RSG) is the central service provider in the Rheinmetall Group. In addition to property management, its duties include the central management and supervision of the employee pension scheme.

Additionally, RSG is a shareholder of Rheinmetall Versicherungsdienst GmbH, which renders insurance brokerage services to the Rheinmetall Group's and some outside companies, too.

The chief task of the property management unit within Rheinmetall Service GmbH is the realty and project development of the former production site in Düsseldorf-Derendorf, which is owned by Rheinmetall Immobilien GmbH (RIG). Of the original approximately 180,000 m^2, plots covering some 120,000 m^2 have already been sold. By securing in advance the necessary planning and construction rights for these projects, it has been possible to achieve a substantial increase in property value. The development plan which was jointly drawn up with the state capital of Düsseldorf for the site, is due to come into force in 2004. Other key activities performed by the property management unit include the marketing of properties for sale as well as looking after and improving properties to be retained within the Rheinmetall Group.

Risk management

Exploiting opportunities posed by market dynamics inevitably entails risk exposure. A key constituent of entrepreneurial drive is to contain such risks while at the same time tenaciously seizing the opportunities.

Groupwide risk management system

The professional and groupwide uniform system for early identification of material and potentially ruinous risks is based on the philosophy of vigilance and structured according to risk policy principles. The system supplements existing budgeting, management and control instruments and is firmly anchored within the Rheinmetall Group's architecture on the basis of clearly defined accountabilities.

The term "risk" refers to the possibility of adverse developments impinging on adopted corporate goals. In order to identify and analyze potential risks, these latter are inventoried and updated as part of the annual planning process which encompasses all the material risks affecting corporate goals and subgoals, the probability of their occurrence, an estimate of the possible loss, a definition of early warning indicators, accountabilities, and appropriate countermeasures.

As part of the monthly reporting mechanisms, the risk reports submitted by the parent and service companies as well as Rheinmetall AG's corporate departments systematically assess existing business risks and categorize or profile these according to probability of occurrence and potential loss. The countermeasures adopted to contain such risks are continuously monitored and, where necessary, reformulated to match any risk reassessments. Rheinmetall AG's Executive Board is regularly briefed by group company controllers on the overall risk situation within the Group. Where necessary, extra suitable action is taken with a view to further containing or limiting detected potential risks. Risks with weighty repercussions are flash-reported to the Executive Board.

The Internal Auditing department periodically reviews the risk management mechanisms for workability, any irregularities, reliability, and economic efficiency. Any flaws or insufficiencies are straightened out in conjunction with the management responsible. The knowledge acquired is then digested and re-fed into the system in order to refine it.

Risk diversification through dissimilar sectors and markets

It is not possible to fully avert market risks linked to economic cycles, rapidly evolving technologies, shorter investment spans, and fiercer competition. Any downturn in the global economy may impinge on the Rheinmetall Group's sales and earnings.

The risk diversification strategy adopted by the Rheinmetall Group with its two largely autonomous core sectors of Automotive (Kolbenschmidt Pierburg Group) and Defence (Rheinmetall DeTec Group) does help to partially balance out any transitory weaknesses within a region or submarket through upturns elsewhere.

Kolbenschmidt Pierburg AG and its subsidiaries develop and manufacture components, modules, and systems for the international motor vehicle industry and as such, their prospects are subject to how the global auto market progresses. However, this group's globalization policy does abate the impact of individual markets and customers on the group's business performance. Added to this is a diversification of customer structure which helps to offset output fluctuations among the OEMs. These latter continue to exercise price pressure. Risk containment is possible by creating additional price/cost latitude, pushing through product and process improvements, enacting CIPs, and observing strict cost management. The accruals for impending losses in the 2003 financial statements adequately provide for potential losses on specific products.

In the Defence sector, Rheinmetall DeTec AG and its subsidiaries are heavily dependent on the defence budget of various countries. The future risk scenario is closely related to limited defence budgets, in turn governed by the prevailing economic situation. Accounting for 43 percent in 2003, domestic business with its stalling defence budget is proving to be especially difficult. Also, the political situation plays a major role in any expansion of exports. Ongoing product innovations and cost-pruning programs are designed to entrench and buttress existing market positions.

Operational and legal risks

Kolbenschmidt Pierburg intends to continue to outpace the international automotive industry by generating better-than-average growth rates. The organic growth budgeted in the sales plans for fiscal 2004 calls for a large number of complex and technologically advanced new-product start-ups which because of their number and scope inherently involve risks. A comprehensive project management scheme is being applied throughout all the phases, from conceptualization, invitation to bid through to series start-up and mass production to ensure that these products translate into profitable growth. In the 2003 financial statements, the accrual for impending losses on individual onerous products or product start-ups adequately provides for any losses.

At to the Defence sector, the financial statements again provide for risks from potentially onerous contracts, while product risks are contained throughout the Rheinmetall DeTec Group by a large number of quality assurance measures which also apply to major suppliers of the Group. All the important locations have been approved according to DIN ISO 9001. Approval procedures, depending on the amounts involved, and perpetual investment controlling are procedures designed to abate any risks relating to expenditure projects.

Environmental risks are limited since the use of hazardous substances is confined. Environmental protection officers ensure that each production facility complies with local regulations.

Reliance on electronic communication technologies grows. The newest security technologies and firewall systems plus virus scanners shield the Rheinmetall Group’s data assets and complex IT systems from attack. The server and storage systems for group-critical applications feature high availability (redundancy) and are configured to prevent failures. Security regulations govern not only the technical configurations of the hardware and software but also include functional security structures and organizational precautions and provisions for minimizing any risks relating to data availability, confidentiality, and integrity.

Sufficient and adequate insurance cover exists for risks arising from damage by natural forces and the ensuing business interruption, as well as for product liability, warranty, indemnity and recall risks. The extent of such cover is regularly reviewed and, where necessary, updated. At the same time, ongoing process reliability and robustness projects as well as extensive quality assurance measures ensure that the mentioned risks do not materialize. Moreover, accruals recognized at sufficient amounts provide for any risks which occur despite these measures and are not or not fully covered by insurance policies (deductible).

Legal and litigation risks emanating from tax, fair trade, patent, antitrust or contract regulations and legislation are downscaled to a minimum exposure wherever possible through ongoing monitoring and in the scope of management discretion.

Proceedings continuing since 1998 are examining the acceptability of the share exchange ratios underlying the merger of Kolbenschmidt and Pierburg. Meanwhile, the expert commissioned by the regional court of Heilbronn has on the basis of provisional figures submitted an interim report that clearly departs from the values stated for the companies merged back in January 1998. After inspecting and reviewing this report, Kolbenschmidt Pierburg AG still sees no reason to refute the share exchange ratios originally worked out which at the time of the merger were calculated by two independent auditing firms and reconfirmed by a court-appointed merger expert. Kolbenschmidt Pierburg is acting on the assumption that the ratios documented in three separate appraisals will withstand final scrutiny. However, in order not to prejudice the ultimate outcome of the proceedings, no further comments are being made at this stage.

The Rheinmetall DeTec Group is at present not involved in any litigation likely to impact materially on its earnings.

Risk management

Regarding the proceedings pending on the reasonableness of the underlying share exchange ratio for KIH stockholders, the latter aim to obtain cash payment in addition to the exchange ratio worked out for the 1999 agreed merger of KIH AG into Aditron AG. Rheinmetall AG's Executive Board regards the action as unjustified and is convinced of the reasonableness of the ratio worked out at the time, and hence rates the risk from the still continuing proceedings as slight.

A number of the minority stockholders of Aditron AG squeezed out by majority stockholder Rheinmetall have attempted to bring an action before a court of law to review the reasonableness of the cash payment allowed for the transfer of shares. Rheinmetall AG's Executive Board regards the action pending before the regional court of Düsseldorf as unjustified and considers any risk as slight.

Hedging against financial risks

Most of the Rheinmetall Group companies are international players and hence exposed to exchange rate fluctuations when operating beyond the eurozone. Suitable and marketable financial derivatives are used exclusively for hedging against currency and interest rate risks. The type and use of such instruments are governed by rules. Open currency positions and exchange rate risks are avoided by refinancing transactions in matching currencies. Corporate Liquidity Management makes sure that at any time there are sufficient funds for the operating business and capital expenditures.

Due to the Rheinmetall Group's global procurement strategies and its far-flung production locations (especially in Automotive), it is proving possible to successively abate the influence of exchange rate fluctuations, especially with respect to the US dollar versus the euro. Financial transactions are contracted solely with banks of prime standing and within predetermined limits. Sufficient accruals provide for losses on long-term contracts or from supply and purchase contracts or agreements. Because of the customer structure, the risk of defaulting debtors is very low. Neither does the Group's business hinge on any specific customers and/or (crisis-prone) regions whose adverse repercussions might jeopardize the survival of the Rheinmetall Group. Other risks (bad debts, warranties, etc.) are adequately provided for in the financial statements.

Statutory auditors' report

The statutory auditors have examined the Rheinmetall Group's risk management system and noted that the Executive Board has taken steps for installing an early risk identification system (ERIS) in line with Art. 91, par. 2 AktG, and that this system is basically suitable to identify in good time any developments that might have a jeopardizing effect on the Group's continued existence as a going concern.

Overall risk assessment by the Executive Board

The current overall review of the risk position has confirmed that the continued existence as a going concern of Rheinmetall AG and its corporate sectors was not at risk in fiscal 2003, whether in terms of assets or liquidity. Nor were any other risks potentially having a material effect on the net assets, financial position and results of operations of Rheinmetall AG or the Group identifiable, nor are any for the future.

Perspectives

Subsequent events

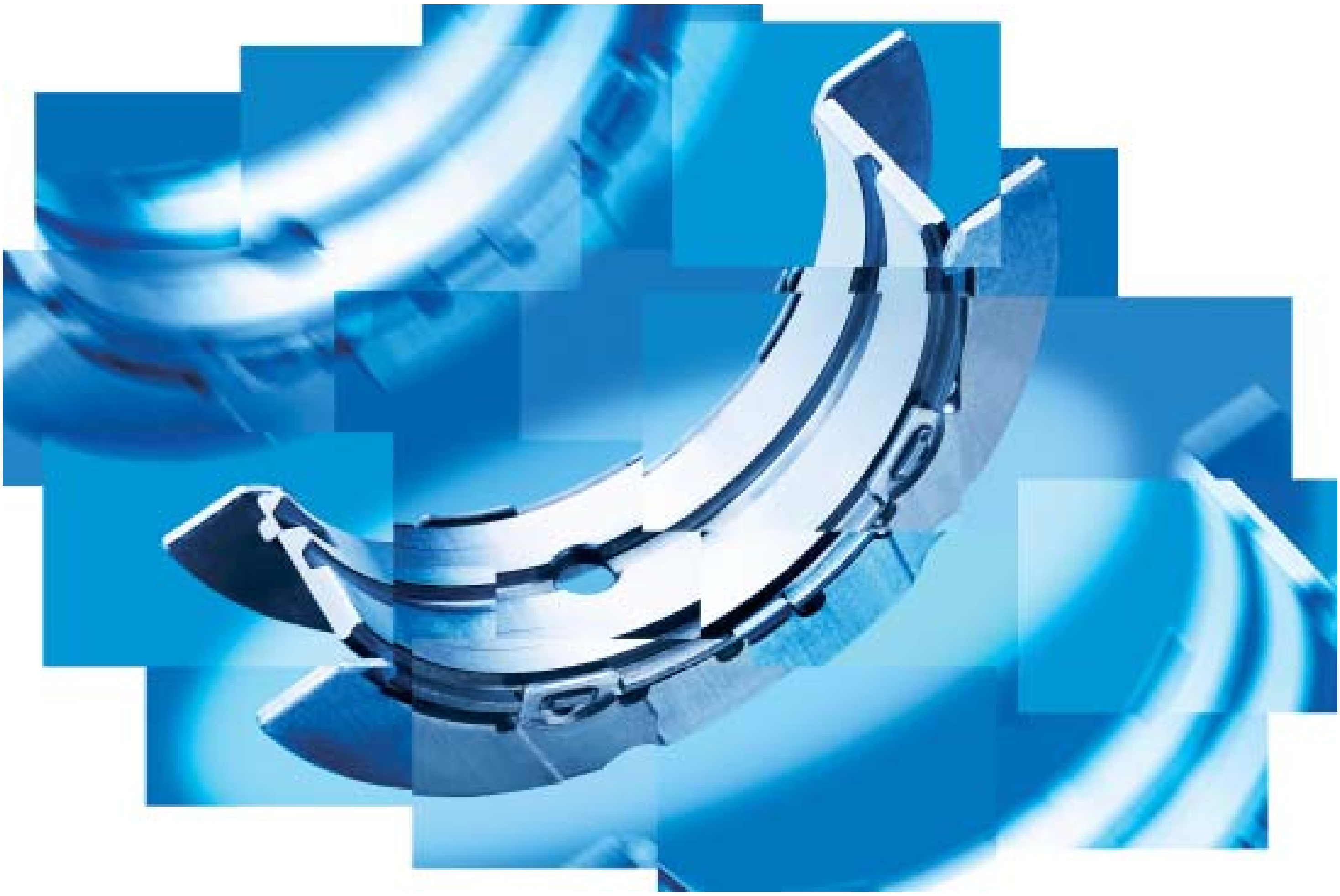
Subsequent to December 31, 2003, Rheinmetall AG sold in February 2004, Neckartenzlingen-based Hirschmann Electronics GmbH & Co. KG to HgCapital, a European private equity investor. The deal, whose consummation is still subject to approval by the relevant cartel authorities, is the closing chapter in the divestment of the Electronics sector.

Also in February this year, Rheinmetall DeTec AG sold the Heidel Group, whose business is nonmilitary, to Frimo Beteiligungs GmbH, Lotte.

In the Automotive sector, Motor Service has through its subsidiary MTS Motorenteile GmbH taken over as of January 2, 2004, the engine parts businesses of E. Trost GmbH & Co. KG Generalvertretungen, Stuttgart, and PV Autoteile GmbH, Duisburg. The moves are intended to broaden market presence even further, add to the existing product range, and improve customer service.

In January 2004, the Pierburg division sold its 49-percent stake in Pierburg Instruments GmbH to the majority shareholder, Graz-based AVL Holding GmbH, the stake being included at equity in the 2003 consolidated balance sheet.

A claim for damages was lodged in January 2004, against one of the subsidiaries of the Automotive sector on account of an aircraft accident in the USA. Claims were also filed against eleven other companies. The statement of the claim does not indicate whether the parts built by the Rheinmetall company caused the accident. The risk from such action is seen as slight and, besides, there is comprehensive insurance cover.



Lead-free and resistant to high pressure and extreme temperatures, products from KS Plain Bearings meet the needs of current and future engine technology

Perspectives

Prospects

By the end of 2003, hopes had risen that the economy would revive in 2004. Many predictions promised a global growth of around 3 percent. Assuming that the US economy develops momentum, the worldwide economy should pick up, too. In Asia, overall economic growth is still robust and even in Japan the apathy of recent years seems to be finally abating. As presently forecasted by experts, Europe, in contrast, will be unable to match this pace, Euroland advancing less than 2 percent and Germany predicted to range between 1.4 and 1.8 percent. Political uncertainties, exchange and interest rate developments or even energy price hikes are all—and remain—possible obstacles in the way of any sustained recovery.

www.bmvg.de/sicherheit/vpr.php

The markets of importance to Rheinmetall are likely to develop as follows:

www.vda.de

www.bundeswehr.de/forces

Present estimates forecast a worldwide total of 61 million cars and light commercial vehicles (LCVs) for 2004, with Asia (again apart from Japan) in particular vigorous. Whereas Japan's output is likely to stall at 10 million units, the rest of Asia is expected to turn out 11 million vehicles (up from 10 million). Following the setback to 16 million in 2003, NAFTA will probably show production advancing to 17 million for this year while the European market, too, may well rebound. Here the number of vehicles manufactured is forecast to climb 2.3 percent to over 17 million units, with Germany, in particular, expected to up its output.

The German government's defence bill for 2004 specifies a ceiling of €24.2 billion in the financial budget, which might grow by up to €520 million thanks to efficiency gains and disposals. The defence capital expenditure budget is €5.9 billion, of which matériel spending will make up €4.0 billion. This is €0.1 billion higher than in 2003. An amount of €1.0 billion has been earmarked for research, development, and tryout. The scope offered by the development and procurement budgets is small since major contracts have already been placed.

In May 2003, Defence Minister Struck redefined defence policy to require a further reorganization of the German armed forces extending to deployment on multinational missions. This steps will lay the groundwork for Germany's agreed participation in the NATO Response Force (NRF) and other crisis missions. It is the various initiatives—especially from the EU and NATO—aimed at transforming the armed forces that generate international defence industry momentum.

Having sold off numerous companies over the past years, Rheinmetall is now squarely aligned with its Automotive and Defence core sectors which hold leading positions in their individual markets. Both these sectors are budgeted to show organic sales growth in fiscal 2004.

At Automotive, the target is to expand business in the North and South American markets as well as set up production bases for Pierburg in Eastern Europe. The Pistons division is seeking to penetrate more deeply into the Japanese market and further develop its operations in Asia, most of all, China. Other targets include further growth in the market for innovative engine blocks and expansion of the domestic aftermarket business.

Assuming that the international side of the business will again branch out, the Defence sector (having pruned its structure in 2003) has also budgeted a rise in sales. While Weapon & Ammunition will very likely not reachieve its 2003 sales due to the disposal of the Heidel Group and the much reduced national procurement program for large-caliber ammunition, the other divisions are looking to show stable to slightly increased sales.

Against the backdrop of sound economic uptrend, Rheinmetall expects for 2004 to improve its EBIT margin. This forward-looking prediction is supported by the budgeted organic growth and the restructuring projects which were successfully completed over the past years in the core operations of Automotive and Defence.

Düsseldorf, March 10, 2004

Rheinmetall Aktiengesellschaft
The Executive Board

Eberhardt Dr. Kleinert Dr. Müller

This annual report contains statements and forecasts referring to the Group's future development which are based on assumptions and estimates by management. If the underlying assumptions do not materialize, the actual figures may differ from such estimates. Elements of uncertainty include changes in the political, economic and business environment, exchange and interest rate fluctuations, the introduction of rival products, poor uptake of new products, and changes in business strategy.

Consolidated financial statements 2003
Rheinmetall AG

Consolidated balance sheet as of December 31, 2003

	ASSETS *€ million*	**12/31/2002**	**12/31/2003**	*Note*
	Fixed assets			
	Intangible assets	345	392	(6)
	Tangible assets	1,332	1,106	(7)
1	Financial assets	55	51	(8)
		1,732	**1,549**	
	Current assets			
	Inventories	902	716	(9)
	less prepayments received	(40)	(27)	
		862	689	
	Trade receivables	662	490	(10)
	All other receivables and sundry assets	383	300	(10)
	Cash & cash equivalents	367	336	(11)
		2,274	**1,815**	
	Income tax assets	**73**	**71**	(12)
	Prepaid expenses & deferred charges	**8**	**7**	
		4,087	**3,442**	

	EQUITY & LIABILITIES *€ million*	**12/31/2002**	**12/31/2003**	*Note*
	Total equity			(13)
	Stockholders' equity (Rheinmetall AG)			
	Capital stock	92	92	
	Additional paid-in capital	208	208	
	Other reserves	113	312	
	Group earnings (after minority interests)	246	63	
		659	**675**	
	Minority interests	210	56	
		869	**731**	
	Accruals			
	Accruals for pensions and similar obligations	660	530	(14)
	Other accruals	581	489	(14)
		1,241	**1,019**	
	Liabilities			
2	Financial debts	668	566	(15)
3	Trade payables	475	455	(15)
3	All other liabilities	744	574	(15)
		1,887	**1,595**	
	Income tax liabilities	**59**	**80**	(16)
	Deferred income	**31**	**17**	(17)
		4,087	**3,442**	

1 *thereof carried at equity: €42 million (virtually unchanged)*

2 *thereof long-term: €519 million (down from €581 million)*

3 *prior-year data adjusted*

Consolidated income statement for fiscal 2003

	€ million	2002	2003	Note
	Net sales	**4,571**	**4,248**	(18)
	Net inventory changes, other work and material capitalized	(64)	26	(19)
	Total operating performance	**4,507**	**4,274**	
	Other operating income	517	249	(20)
	Cost of materials	(2,077)	(2,014)	(21)
	Personnel expenses	(1,447)	(1,339)	(22)
	Amortization/depreciation/write-down	(309)	(242)	(23)
	Other operating expenses	(797)	(722)	(24)
	Operating result	**394**	**206**	
	Net interest expense	(102)	(84)	(25)
1	Net investment income and other financial results	(2)	(2)	(26)
	Net financial result	**(104)**	**(86)**	
2	**Earnings before taxes (EBT)**	**290**	**120**	
	Income taxes	(16)	(52)	(27)
	Group net income	**274**	**68**	
	Minority interests	(28)	(5)	(28)
	Group earnings (after minority interests)	**246**	**63**	

1 *thereof profit from financial assets carried at equity: €9 million (up from €8 million)*

2 *thereof EBT from discontinued operations: €22 million (down from €303 million); cf. Note (33)*

	2002	2003	Note
EpS, common stock (after goodwill amortization)	€6.81	€1.72	(29)
EpS, preferred stock (after goodwill amortization)	€6.87	€1.78	(29)
EpS, common stock (before goodwill amortization)	€7.89	€2.56	(29)
EpS, preferred stock (before goodwill amortization)	€7.95	€2.62	(29)
EBIT	392	204	
EBITDA	701	446	

Consolidated statement of cash flows for fiscal 2003

€ million	2002	2003
Cash & cash equivalents at Jan. 1 (BoP)	**223**	**367**
Group net income	274	68
Amortization/depreciation/write-down/write-up of intangibles and tangibles	309	238
Change in pension accruals	4	2
Cash flow	**587**	**308**
Net result from fixed-asset disposal	(333)	(35)
Change in other accruals	55	(7)
Change in inventories	66	(6)
Change in receivables, liabilities (excl. financial debts) and prepaid & deferred items	(5)	46
Other noncash expenses and income, net	(29)	(5)
[1] **Net cash provided by operating activities**	**341**	**301**
Cash outflow for additions to tangible and intangible assets	(248)	(203)
Cash inflow from the disposal of tangible and intangible assets	31	47
Cash outflow for additions to consolidated subsidiaries and financial assets	(178)	(148)
Cash inflow from the disposal of consolidated subsidiaries and financial assets	427	115
Net cash provided by/(used in) investing activities	**32**	**(189)**
Dividend paid out by Rheinmetall AG	(17)	(24)
Other profit distribution	(9)	(5)
Financial debts raised	8	6
Financial debts redeemed	(210)	(118)
Net cash used in financing activities	**(228)**	**(141)**
Cash-based change in cash & cash equivalents	**145**	**(29)**
Parity-related change in cash & cash equivalents	(1)	(2)
Total net change in cash & cash equivalents	**144**	**(31)**
Cash & cash equivalents at Dec. 31 (EoP)	**367**	**336**

For comments on the cash flow statement, see Note (31).

[1] *included are*
interest paid at €43 million (down from €50 million)
income taxes paid at €40 million (up from €30 million)

Statement of changes in equity

€ million

	Capital stock	Additional paid-in capital	*Reserves retained from earnings*	*Currency translation differences*	*Reserves from fair and other valuation*	All other reserves	Group earnings after minority interests	**Stockholders' equity (Rheinmetall AG)**	Minority interests	**Total equity**
Balance at January 1, 2002	**92**	**208**	*66*	*(6)*	*69*	**129**	**21**	**450**	**267**	**717**
Dividend payments	--	--	*(17)*	--	--	(17)	--	(17)	(9)	(26)
Currency translation differences	--	--	--	(24)	--	(24)	--	(24)	(1)	(25)
Changes in consolidation group	--	--	*12*	--	--	12	--	12	(68)	(56)
Transfer to/from reserves	--	--	*21*	--	--	21	(21)	--	--	--
Other comprehensive income	--	--	*(4)*	--	*(4)*	(8)	--	(8)	(7)	(15)
Group net income	--	--	--	--	--	--	246	246	28	274
Balance at December 31, 2002	**92**	**208**	*78*	*(30)*	*65*	**113**	**246**	**659**	**210**	**869**
Dividend payments	--	--	*(24)*	--	--	(24)	--	(24)	(5)	(29)
Currency translation differences	--	--	--	*(11)*	--	(11)	--	(11)	(2)	(13)
Changes in consolidation group	--	--	*(10)*	--	--	(10)	--	(10)	(153)	(163)
Transfer to/from reserves	--	--	*246*	--	--	246	(246)	--	--	--
Other comprehensive income	--	--	*(2)*	--	--	(2)	--	(2)	1	(1)
Group net income	--	--	--	--	--	--	63	63	5	68
Balance at December 31, 2003	**92**	**208**	*288*	*(41)*	*65*	**312**	**63**	**675**	**56**	**731**

For comments on equity, see Note (13).

Notes (Group)
Segment reports according to IFRS

Primary segments *€ million*	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**
Corporate sectors	Automotive		Defence		Electronics		Others/ Consolidation		**Group**	
Net external sales	1,883	1,884	1,675	1,602	775	478	238	284	**4,571**	**4,248**
Intersegment transfers	--	--	2	3	27	23	(29)	(26)	**--**	**--**
Total segment sales	1,883	1,884	1,677	1,605	802	501	209	258	**4,571**	**4,248**
P/L from investees stated at equity	2	8	--	--	--	--	6	1	**8**	**9**
Income from write-up	--	--	--	--	--	--	--	3	**--**	**3**
Write-down	(13)	(6)	(15)	(7)	(9)	--	(16)	(4)	**(53)**	**(17)**
Segment EBIT	79	98	71	68	247	42	(5)	(4)	**392**	**204**
Cash flow from operating activities	215	174	79	159	60	22	(13)	(54)	**341**	**301**
Segment assets	1,257	1,246	1,779	1,459	313	144	299	186	**3,648**	**3,035**
thereof investment book values at equity	*28*	*37*	*2*	*2*	*2*	*3*	*10*	--	***42***	***42***
Segment liabilities	684	674	1,428	1,189	203	148	176	54	**2,491**	**2,065**
Segment expenditures	161	150	70	109	117	27	24	37	**372**	**323**

Secondary segments *€ million*	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**
Regions	Germany		Other Europe		North America		Asia		Other Regions/ Consolidation		**Group**	
Net external sales by customer location	1,720	1,649	1,852	1,706	571	486	270	280	158	127	**4,571**	**4,248**
in % of Group sales	37.6	38.8	40.5	40.2	12.5	11.4	5.9	6.6	3.5	3.0	**--**	**--**
Segment assets	2,354	2,055	858	787	276	235	15	29	145	(71)	**3,648**	**3,035**
Segment expenditures	240	210	75	71	45	23	2	15	10	4	**372**	**323**

For comments on the segment reports according to IAS, see Note (32).

Segment report according to management structure

€ million		Automotive 2002	Automotive 2003	Defence 2002	Defence 2003	Electronics 2002	Electronics 2003	Others/ Consolidation 2002	Others/ Consolidation 2003	**Group 2002**	**Group 2003**
Corporate sectors											
Balance sheet (Dec. 31)											
Total equity	(1)	333	363	436	370	409	26	(309)	(28)	**869**	**731**
Pension accruals	(2)	273	256	265	212	60	37	62	25	**660**	**530**
Net financial debts	(3)	166	105	(100)	(127)	(291)	(16)	526	268	**301**	**230**
Capital employed (CE)	(1)+(2)+(3)	772	724	601	455	178	47	279	265	**1,830**	**1,491**
Average CE	(4)	827	748	585	528	216	113	325	272	**1,953**	**1,661**
Income statement											
Net external sales		1,883	1,884	1,675	1,602	775	478	238	284	**4,571**	**4,248**
Intersegment transfers		--	--	2	3	27	23	(29)	(26)	**--**	**--**
Total segment sales		1,883	1,884	1,677	1,605	802	501	209	258	**4,571**	**4,248**
thereof Germany (in %)		*33.5*	*32.1*	*44.1*	*43.1*	*39.1*	*51.5*	--	--	*37.6*	*38.8*
thereof abroad (in %)		*66.5*	*67.9*	*55.9*	*56.9*	*60.9*	*48.5*	--	--	*62.4*	*61.2*
EBITDA		234	239	150	138	359	64	(42)	5	**701**	**446**
Amortization/depreciation/write-down		(137)	(136)	(78)	(69)	(32)	(19)	(62)	(18)	**(309)**	**(242)**
Segment EBIT (by management structure)	(5)	97	103	72	69	327	45	(104)	(13)	**392**	**204**
Net interest expense		(37)	(31)	(22)	(23)	(9)	(4)	(34)	(26)	**(102)**	**(84)**
EBT		60	72	50	46	318	41	(138)	(39)	**290**	**120**
Income taxes		(23)	(29)	(5)	(22)	(7)	(4)	19	3	**(16)**	**(52)**
Net income/(net loss)		37	43	45	24	311	37	(119)	(36)	**274**	**68**
EBIT margin (in %)		5.2	5.5	4.3	4.3	40.8	9.0	--	--	**8.6**	**4.8**
Other data											
ROCE (in %)	(5)/(4)	11.8	13.8	12.3	13.0	151.6	39.8	--	--	**20.1**	**12.3**
Segment expenditures		144	127	48	46	41	27	15	3	**248**	**203**
Order intake		1,917	1,860	1,861	1,473	835	510	227	285	**4,840**	**4,128**
Order backlog at Dec. 31		339	314	3,649	2,748	144	73	33	8	**4,165**	**3,143**
Prepayments received		7	17	691	478	2	--	6	(1)	**706**	**494**
Employees at Dec. 31		11,535	11,316	8,828	7,435	4,310	1,734	1,276	403	**25,949**	**20,888**

For comments on the segment reports according to management structure, see Note (32).

Notes (Group)
Fixed-asset analysis

Fixed-asset analysis *€ million*

	Gross values				
	1/1/2003	Additions	Disposals [1]	Book transfers	Changes in consolidation group/shareholding
Intangible assets					
Development costs and other internally created intangible assets	17	10	--	1	4
Concessions, franchises, industrial property rights and licenses	93	13	11	12	(24)
Goodwill	459	--	2	--	54
Badwill from consolidation	(32)	--	(6)	--	11
Prepayments on intangibles	12	3	--	(11)	--
	549	26	7	2	45
Tangible assets					
Land, equivalent titles, and buildings (incl. buildings on leased land)	1,145	11	27	1	(127)
Investment properties	91	--	5	5	(3)
Production plant and machinery	1,674	64	52	43	(86)
Other plant, factory and office equipment	707	33	56	20	(167)
Prepayments on tangibles, construction in progress	91	69	2	(71)	(12)
	3,708	177	142	(2)	(395)
Financial assets					
Shares in nonconsolidated Group companies	--	--	--	--	--
Loans to nonconsolidated Group companies	--	--	--	--	--
Shares in joint ventures (at equity)	54	9	--	8	(40)
Shares in associated affiliates (at equity)	21	--	--	(8)	(2)
Loans to joint ventures and associated affiliates	--	--	--	--	--
Other long-term securities	17	2	--	--	(6)
Other long-term loans	5	--	1	--	--
	97	11	1	--	(48)
Total	**4,354**	**214**	**150**	**--**	**(398)**

[1] *including revaluation-related write-down and write-up*

		Amortization/depreciation/write-down								Net values	
Currency translation differences	**12/31/ 2003**	1/1/2003	Additions	Disposals	Book transfers	Write-up	Changes in consoli-dation group/share-holding	Currency translation differences	**12/31/ 2003**	12/31/ 2002	**12/31/ 2003**
--	32	8	4	--	--	--	--	--	12	9	20
(1)	82	73	12	9	--	--	(21)	(1)	54	20	28
(2)	509	148	31	2	--	--	(12)	(1)	164	311	345
--	(15)	(25)	--	(6)	--	1	10	--	(10)	(7)	(5)
--	4	--	--	--	--	--	--	--	--	12	4
(3)	612	204	47	5	--	1	(23)	(2)	220	345	392
(22)	981	488	28	4	--	--	(54)	(12)	446	657	535
(3)	85	54	2	3	--	3	(2)	(1)	47	37	38
(50)	1,593	1,260	110	47	(3)	--	(58)	(35)	1,227	414	366
(7)	530	564	55	51	3	--	(140)	(6)	425	143	105
(4)	71	10	--	--	--	--	--	(1)	9	81	62
(86)	3,260	2,376	195	105	--	3	(254)	(55)	2,154	1,332	1,106
--	--	--	--	--	--	--	--	--	--	--	--
--	--	--	--	--	--	--	--	--	--	--	--
--	31	31	--	--	--	1	(30)	--	--	23	31
--	11	2	--	--	--	--	(2)	--	--	19	11
--	--	--	--	--	--	--	--	--	--	--	--
--	13	8	2	--	--	3	--	--	7	9	6
--	4	1	--	--	--	--	--	--	1	4	3
--	59	42	2	--	--	4	(32)	--	8	55	51
(89)	**3,931**	**2,622**	**244**	**110**	**--**	**8**	**(309)**	**(57)**	**2,382**	**1,732**	**1,549**

Notes (Group)
Accounting principles

(1)
General

The consolidated financial statements of Rheinmetall AG and its subsidiaries for the fiscal year 2003 have been prepared in accordance with all International Financial Reporting Standards (IFRS) and Interpretations of the International Accounting Standard Board (IASB) effective at balance sheet date. These financial statements conform with the 7th EC Directive as interpreted by the Contact Committee for Accounting Directives of the European Commission (Directive 83/349 EEC).

For enhanced transparency of presentation, certain items of the consolidated balance sheet and income statement have been subsumed in captions but are broken down and detailed further below in these notes. The consolidated income statement has been prepared in the total-cost format. Additional financial statements include a consolidated statement of cash flows and a statement of changes in equity.

The consolidated financial statements are presented in euro (€). Amounts are almost throughout indicated in € million (including prior-year figures).

With its IFRS-based consolidated financial statements, Rheinmetall AG has exercised the exemption option under the terms of Art. 292a HGB, viz. to draw up the consolidated accounts in accordance with internationally accepted accounting principles in lieu of consolidated financial statements according to German commercial accounting regulations. The assessment of whether the consolidated financial statements and group management report meet the prerequisites of Art. 292a HGB has been made in conformity with the GASC interpretation in German Accounting Standard GAS-1. The present consolidated statements substantially reflect the following accounting and valuation methods in derogation of the German Commercial Code (HGB):

– translation of non-euro receivables and payables at the current closing rate and recognition in net income of the resulting translation differences (IAS 21)

– recognition at fair value of certain financial instruments (IAS 39)

– capitalization of internally created intangible assets (IAS 38)

– fair valuation of essential plots of land according to the alternative revaluation method (IAS 16)

– realization of profits according to the percentage of completion (PoC) from long-term manufacturing contracts with customers (IAS 11)

– discounting of noncurrent accruals (IAS 37)

– waiver of providing for accrued liabilities if the probability of accrual utilization is below 50 percent (IAS 37)

– accounting for deferred taxes according to the liability method (IAS 12)

– capitalization of the asset and recognition of the residual liability under capital leases according to the definition criteria of IAS 17

– measurement of pension accruals according to the projected unit credit (PUC) method with due regard to future pay rises and the corridor rule of IAS 19.

The fiscal year of Rheinmetall AG and its subsidiaries equals the calendar year. Hirschmann Electronics GmbH & Co. KG, a Neckartenzlingen-based limited partnership and subsidiary, has claimed the option of Art. 264b HGB to be exempted from the publication of its own consolidated statements. Rheinmetall AG (Local Court of Registration: Düsseldorf) has its registered office in Düsseldorf at Rheinmetall Allee 1. Top-tier parent company is Röchling Industrie Verwaltung GmbH, Mannheim.

(2)
Consolidation group

Besides Rheinmetall AG, the consolidated financial statements include all German and foreign subsidiaries in which Rheinmetall AG holds the majority of voting rights (whether directly or indirectly) or whose financial and business policies or otherwise controlled by the Group. Principally, companies are initially consolidated or deconsolidated when control is transferred. Associated affiliates (i.e., companies in which a stake between 20 and 49 percent is owned and over which a controlling influence is exercised) and joint ventures (held at 50 percent and jointly managed) are stated at equity.

For lack of materiality, 2 insignificant subsidiaries (down from 4) have not been included in the consolidated financial statements.

Consolidation group – included companies

	12/31/2002	Additions	Disposals	**12/31/2003**
Fully consolidated companies				
Germany	87	14	27	74
abroad	70	14	31	53
	157	**28**	**58**	**127**
Investments stated at equity				
Germany	8	2	3	7
abroad	8	2	1	9
	16	**4**	**4**	**16**

In the year under review, 28 subsidiaries were newly consolidated while 58 companies (including 31 non-German) left the consolidation group.

The shares (newly or additionally) acquired in the year under review in the following fully consolidated companies are reportable in particular:

– Oerlikon Contraves AG, Zurich, Switzerland: stake increased from 80 to 100 percent in January 2003, at a price of €43 million

– EMG EuroMarine Electronics GmbH, Hamburg, Germany: 50-percent stake in the capital stock increased to 100 percent in February 2003, at a price of €18 million

– Microtechno Corporation, Japan: pistons operations taken over from Mazda in February 2003, at a price of €9 million

– Aditron AG, Düsseldorf, Germany: stake in the capital stock increased, also by squeeze-out, in June 2003, at a price of €11 million

– Jagenberg AG, Neuss, Germany: 88-percent stake in the capital stock increased to 94 percent by August 2003, at a price of €3 million

– Preh-Werke GmbH & Co. KG, Bad Neustadt/Saale, Germany: 75-percent interest in the limited partnership's capital increased to 100 percent in September 2003, at a price of €17 million

– Kolbenschmidt Pierburg AG, Düsseldorf, Germany: 80-percent stake in the capital stock increased to 95 percent by December 2003, at a price of €70 million

– Further investments, at a total price of €1 million.

In the year under review, a total €172 million was spent to acquire shares in fully consolidated subsidiaries (up from €168 million).

Notes (Group)
Accounting principles

The following disposals of shares in fully consolidated subsidiaries are significant:

- Sale and transfer of the remaining operations of the Jagenberg Group including Jagenberg AG (January to August 2003) against payment by Rheinmetall of €2 million
- Sale and transfer of Preh-Werke GmbH & Co. KG, Bad Neustadt/Saale, in October 2003, at a price of €74 million
- Sale and transfer of the operations of Hamburg-based STN Atlas Marine Electronics GmbH in November 2003, at an undisclosed price (as covenanted)
- Sale and transfer of Hirschmann Austria GmbH, Rankweil, in June 2003, at an undisclosed price (as covenanted)
- Further divestments at a total €16 million

The purchase prices negotiated for the disposal of fully consolidated subsidiaries totaled €200 million (down from €438 million). Moreover, the Naval Systems business was spun off in August 2003 from STN Atlas Elektronik GmbH, Bremen (now renamed Rheinmetall Defence Electronics).

The acquisitions and divestments in the (prior) period impacted on the assets and liabilities as of December 31 and major lines of the consolidated income statement as follows:

Acquisitions/divestments *€ million*	2002	**2003**
Fixed assets	(39)	(133)
Current assets	(207)	(499)
Accruals for pension and similar obligations	(14)	(125)
Other accruals	(59)	(70)
Financial debts	(29)	16
Trade payables and all other liabilities	(108)	(238)

Acquisitions/divestments *€ million*	2002	**2003**
Net sales	(319)	(300)
Operating result	(34)	10
EBT	(33)	16
Net income	(26)	13

All major consolidated subsidiaries and the material investees stated at equity are listed separately after these notes. A comprehensive listing of the shareholdings of Rheinmetall AG has been deposited with the Commercial Register of the Local Court of Düsseldorf (HRB 39401).

(3)
Consolidation principles

The financial statements of consolidated German and foreign companies are prepared in accordance with groupwide uniform accounting and valuation methods.

Subsidiaries included for the first time are consolidated according to the purchase method, specifically the book value method under the terms of IAS 22, by offsetting the cost of shares acquired against the subsidiaries' prorated equity. Any difference between cost and prorated equity is, if based on hidden reserves or burdens, allocated at the Group's percentage shareholding in such hidden reserves or burdens to the subsidiaries' assets and liabilities. Any residual net equity under or over cost is capitalized as goodwill or badwill within intangible assets. Goodwill is amortized over its estimated useful life, while badwill is released to other operating income in accordance with IAS 22. Any net equity under cost from pre-1995 acquisitions had been offset against the Group's reserves retained from earnings.

Minority interests in the consolidatable equity of subsidiaries (including those in profit and loss) are recognized and disclosed as such in the balance sheet.

Expenses and income from intragroup transactions, as well as intercompany receivables and payables are eliminated in consolidation. Intragroup trade transfers are based on fair market prices as well as intragroup transfer prices as if at arm's length. Intercompany profits and losses are eliminated unless insignificant. Deferred taxes are recognized for temporary differences from consolidation.

Shares in associated affiliates and joint ventures are principally stated at equity. Starting from the historical cost of the shares as of the date of their acquisition, the investment book value is increased or decreased to reflect such changes in the equity of these investees/joint ventures as are allocable to the Rheinmetall Group.

To determine the goodwill (if any) of investees carried at equity, principles analogous to consolidation are adopted, capitalized goodwill being mirrored in the investment book value and goodwill amortization recognized in net investment income.

(4)
Currency translation

The functional currency concept has been adopted to translate the annual financial statements of non-German group companies into euros. As a rule, their functional currency equals the local currency. Therefore, assets and liabilities are translated at the mean current, and the income statements at the annual average, rates. The translation differences resulting herefrom are recognized in, and only in, equity. Goodwill created from the capital consolidation of non-German companies is carried at amortized historical cost and translated at the current rate. The annual financial statements of a small Turkish subsidiary were prepared on the basis of the historical cost concept and adjusted in accordance with IAS 29, Financial Reporting in Hyperinflationary Economies.

In the local-currency financial statements of consolidated companies, currency receivables and payables as well as cash & cash equivalents are all translated at the current closing rate. Currency translation differences are duly recognized in the net financial result.

Notes (Group)
Accounting principles

(5)
Accounting and valuation methods

Rheinmetall AG's consolidated financial statements are prepared on the basis of groupwide uniform, consistently applied accounting and valuation principles. The proratable equity of investees carried at equity is valued according to analogous principles.

Intangible assets

Purchased intangible assets are capitalized at (acquisition) cost, internally created intangibles from which the Group is believed to derive future economic benefits and which can reliably be measured are recognized at production cost, either type of intangible asset being amortized by straight-line charges over the estimated useful life. Production cost covers all costs directly allocable to the production process, including any proratable production-related overheads. No cost of finance is capitalized. R&D costs are principally expensed. However, development costs are capitalized and amortized on a straight-line basis if a newly developed product or process can be clearly defined, technologically realized and used either internally or is destined for marketing (IAS 38), and if there is a reasonable assurance that its costs will be recovered by future cash inflows. If certain factors hint at an impairment and the recoverable amount is below amortized cost, an intangible asset is written down. Wherever the reason for write-down has ceased to exist, the charge is reversed and the asset written up accordingly.

The following unchanged useful lives underlie amortization:

Intangible assets *Years*	2002	**2003**
Concessions, franchises, and industrial property rights	3-15	3-15
Goodwill	15-20	15-20
Development costs	5	5-7

The period of benefit from goodwill is estimated with due regard to the benefits expected from the market position achieved through the acquisition and from the acquiree's value-adding potential.

Tangible assets

Tangible assets are carried at depreciated cost less any write-down. The production cost of internally made tangible assets comprises all costs directly allocable to the production process, including the proratable production-related overheads. Borrowing costs are not capitalized as part of cost. Tangible assets are principally depreciated on a straight-line basis over their estimated useful lives unless in exceptional cases another method better reflects the pattern of use.

The following unchanged asset depreciation ranges (ADR) apply to property, plant & equipment within tangible assets:

Tangible assets	Years
Buildings	20–50
Other structures	8–30
Equivalent titles	5–15
Production plant and machinery	3–20
Other plant, factory and office equipment	3–15

Public subsidies, as well as grants which have been received from customers and substantially qualify as investment grants, are directly offset against acquisition cost.

Essential plots of land owned for business purposes are stated according to the alternative revaluation method of IAS 16 at their fair values, which regularly equal market values.

Investment properties continue to be carried at depreciated cost. The market value of investment properties, determined according to generally accepted valuation techniques and substantially based on values indicated by an independent appraiser, is stated in Note (7).

Tangible assets obtained under capital leases are capitalized at the lower of their fair values or the present value of minimum lease payments and depreciated over the shorter of their estimated useful lives or underlying lease terms (IAS 17). If certain factors hint at an impairment and the recoverable amount is below depreciated cost, a tangible asset is written down. Wherever the reason for write-down has ceased to exist, the charge is reversed and the asset written up accordingly.

Financial assets

The shares in nonconsolidated group companies and in associated affiliates other than stated at equity and the other long-term securities, all shown as financial assets, are carried at their fair values since they are throughout available for sale. Where such fair market values are not reliably determinable, assets are carried at amortized cost. Gains and losses, while unrealized, are shown in the reserves from fair and other valuation but, upon financial-asset disposal, are recognized in net income. However, if and when substantiated evidence hints at an impairment, even unrealized losses are recognized in net income.

Initial measurement is based on the value at settlement date.

In accordance with IAS 39, long-term loans bearing interest at fair market rates are carried at amortized cost, whereas non- or low-interest loans are discounted and shown at their present values.

Inventories and prepayments received

Inventories are recognized at cost, as a rule applying the average-price method to acquisition cost whereas production cost includes direct costs plus any portions of indirect materials, indirect manufacturing costs (labor, etc.), as well as production-related depreciation and pension expenses, always based on normal workloads, but cost always excludes any borrowing costs (IAS 23). Risks inherent in inventories due to reduced utility or to obsolescence are adequately allowed for. If the net realizable value (NRV) of any inventories at balance sheet date is below their carrying value, such inventories are written down to NRV.

If the NRV of inventories previously written down has risen, the ensuing write-up is principally offset against cost of materials (raw materials and supplies) or shown as increase in inventories of finished products and work in process (WIP).

Prepayments received from customers for contracts other than long-term manufacturing or construction contracts under the terms of IAS 11 are, if production cost has already been incurred, openly deducted directly from inventories, any other prepayments being recognized as liabilities.

Notes (Group)
Accounting principles

PoC accounting

Where the criteria and requirements of IAS 11 are met, longer-term manufacturing orders or construction contracts from customers are recognized in accordance with their percentage of completion. This method implies that the production cost incurred, plus a markup in line with the percentage of completion, is shown as receivable under l/t manufacturing contracts and within net sales. As a rule, the PoC is determined on a cost-to-cost basis, i.e., at the ratio the expenses incurred bear to anticipated total expenses. Expected losses on l/t manufacturing contracts (so-called onerous contracts) are either covered by an appropriate write-down or else provided for, all with due regard to all foreseeable risks. Prepayments received are directly offset against the receivables under l/t manufacturing contracts. If resulting in a negative balance, the corresponding liability is recognized as payable under l/t manufacturing contracts.

Receivables and sundry assets

Receivables and sundry assets are capitalized at cost. Adequate allowances provide for bad debts and doubtful accounts.

Since the short-term securities are throughout available for sale they are stated at fair value as of the balance sheet date. Changes in fair value are not recognized in income until realized but shown within equity. However, if a value has been impaired and fallen below cost, even unrealized losses are recognized in net income.

Deferred taxes

In accordance with IAS 12, deferred taxes are duly recognized on the temporary differences between the values of assets and liabilities in the consolidated balance sheet and those in the individual companies' tax accounts. Deferred tax assets also include tax reduction claims from the expected future utilization of tax loss carryovers (if their realization is reasonably certain). Deferred taxes are determined by applying the local tax rates current or reliably anticipated in each country at the balance sheet date.

An unchanged 40 percent has been applied to calculate German deferred taxes (corporate income tax, solidarity surtax thereon and municipal trade tax on income). Deferred taxation rates outside of Germany range between 25 and 38 percent, comparing with the year-earlier range of 15 to 40 percent.

Enacted on December 22, 2003, the so-called Basket II of bills and acts (inter alia, amending municipal trade taxation) has changed the system of the tax treatment of losses in Germany. As from January 2004, only a maximum 60 percent of a tax loss carryover from prior years may be offset against a corporation's taxable income (a base of €1 million of income remaining offsettable without limitation or restriction). This rule applies analogously to losses carried over for municipal trade tax purposes.

Also amended was the previous tax rule which exempted capital gains from the disposal of shareholdings in corporations. As from January 1, 2004, five percent of the capital gain must be added as nondeductible business expenses to taxable income.

In the year under review, the amended legislation did not impact on deferred tax assets or liabilities. The deferred tax liabilities of €6 million for the €301 million temporary differences of shares in group companies and associated affiliates were not recognized since Rheinmetall can control the reversal of such differences and the reversal is not probable in the foreseeable future.

Accruals

As required by IAS 19, accruals for pensions and similar obligations are determined, where defined benefit obligations (DBO) are involved, according to the projected unit credit (PUC) method, which is predicated on assumptions such as mortality, expected future pay and pension increases, plan beneficiary turnover rates, interest rate variations, as well as other actuarial parameters. The actuarial gains and losses ensuing from differences between actuarial assumptions and actual trends of the underlying parameters give rise to a gap between the present value of the DBO and the pension liabilities accrued in the balance sheet. Actuarial gains and losses outside a 10-percent corridor of the DBO's present value are distributed over the average residual service years of employees. The fair market value of any existing pension fund assets is deducted from pension accruals. Payments to defined contribution plans (DCP), under which the company incurs no obligations other than to pay the contributions to earmarked pension funds, are recognized in net income in the year of their incurrence.

The remaining accruals according to IAS 37 provide at balance sheet date for all identifiable legal and constructive commitments and obligations to third parties if based on past transactions or events and if their amount, due date or maturity is uncertain. Accruals are measured at the best estimate of their settlement amounts. Noncurrent accruals are shown, if the effect of discounting is significant, at the settlement amount discounted as of balance sheet date. The settlement amount also accounts for identifiable future cost increases.

Liabilities

Pursuant to IAS 39, liabilities are measured at amortized cost, which as a rule equals the settlement or repayment amount.

Liabilities under capital leases are recognized at the present value of future lease payments.

Prepaid and deferred items

Such items are shown to appropriately recognize pro rata temporis (p.r.t.) prepaid rents, royalties, license fees, interest, insurance premiums, etc.

Public grants other than for capital expenditures and subsidies for expenses are recognized as deferred income in line with the options of IAS 20 and realized when the corresponding expenses are incurred.

If the selling price of an asset disposed of under a sale-leaseback transaction exceeds its net book value (depreciated cost), the gain from disposal is recognized as deferred income and amortized to income over the noncancelable initial lease term.

Notes (Group)
Accounting principles

Contingent liabilities/assets

Contingent liabilities are possible or existing obligations arising from past events or indicating that an outflow of resources is unlikely.

Contingent assets are possible assets whose existence hinges on the occurrence (or otherwise) of one or several future events not wholly controllable by Rheinmetall.

Contingent liabilities and assets are disclosed in the notes at their probable settlement amounts.

Income and expenses

Net sales and other operating income are recognized upon performance of the contract for goods/services or upon passage of risk to the customer. Under longer-term manufacturing or construction contracts with customers, sales are prorated according to the percentage of completion. Operating expenses are recognized when caused or when the underlying service, etc. is used. Interest income and expenses are recognized on an accrual basis.

Derivative financial instruments

Companies of the Rheinmetall Group use financial derivatives solely to hedge balance sheet items and future cash flows.

Pursuant to IAS 39, Financial Instruments, all financial derivative are recognized at cost at the trading/contracting date and thereafter remeasured at their fair values. Financial derivatives with a positive or negative fair value are disclosed under sundry assets or all other liabilities, respectively.

Changes in the fair value of financial derivatives are principally recognized in net income immediately unless an effective hedge exists that satisfies the criteria of IAS 39. If the derivative is a cash flow hedge (CFH) and hence used to effectively hedge expected future cash inflows/outflows, changes in the financial derivative’s fair value are recognized under the other reserves only and not in net income. In this case, the changes in the derivative’s value would not impact on net income until after the hedged underlying transaction has fallen due or been settled.

Changes in the value of financial derivatives used in fair value hedges (FVHs) to effectively hedge the fair value of recognized assets and liabilities are posted to net income as are any changes in the hedged assets or liabilities (where appropriate, by adjusting their book values), with the result that the compensatory effects are all reflected in the income statement.

The ineffective portion of a hedge is recognized in net income.

Notes to the balance sheet

(6)
Intangible assets

In the year under review, non-contracted R&D expenses of €189 million were incurred (down from €208 million).

Operating expenses included the following R&D-related items:

Thereof, development costs of €10 million met the capitalization criteria according to IFRS (up from €4 million).

R&D costs *€ million*

	2002	2003
Research costs and noncapitalized development costs	204	179
Amortization of capitalized development costs	2	4
Total R&D costs expensed	**206**	**183**

Total amortization of intangible assets of €47 million (down from €55 million) includes write-down of €7 million (down from €17 million) which was charged to the goodwill from the acquisition of Jagenberg stock and to that of the Heidel Group within Defence.

The badwill from capital consolidation was amortized to other operating income at €1 million (down from €2 million), the remaining badwill being amortized by fiscal 2008.

(7)
Tangible assets

Depreciation includes write-down at €10 million (down from €36 million), of which €2 million (down from €34 million) was charged to land and buildings, another €7 million (up from €2 million) to production plant and machinery, and €1 million to other plant, factory and office equipment.

In accordance with the revaluation method of IAS 16, essential business plots of land have been stated at their fair values, which principally equal market values. Valuation of the land situated in Germany and abroad, which had been revalued on the basis of independent appraisal reports prepared as of December 31, 2002, was updated in 2003 and stepped up the essential land's net carrying amounts as of December 31, 2003, by €102 million (down from €116 million). To the extent that the remeasured fair value of the land falls below depreciated cost, application of the revaluation method results in write-down (nil in 2003, down from €7 million) which is recognized in net income. Regarding the development of the revaluation reserve, see the comments on total equity.

By definition, investment properties are held to earn rental income or for long-term capital appreciation and not used for production or administrative purposes. Investment properties are valued at depreciated cost. The investment properties have a fair value of €51 million (down from €54 million). In the year under review, rental income of €4 million (unchanged) was earned which contrasts with direct operating expenses of a €2 million (up from €1 million).

The disposition of €37 million of tangible assets (down from €55 million) is restricted by land charges, similar encumbrances and the assignment as security. Moreover, standard commercial liens totaling €105 million (down from €143 million) rest on assets held under capital leases and allocable to the Group under the terms of IAS 17, as well as on properties of consolidated special-purpose leasing firms.

Notes (Group)
Notes to the balance sheet

Tangible assets have been capitalized under leases at the following amounts:

Capitalized tangible assets under leases *€ million*

	12/31/2002			**12/31/2003**		
	Capital leases	Consoli-dation of special-purpose leasing firms	Total	Capital leases	Consoli-dation of special-purpose leasing firms	Total
Land and buildings	35	75	110	26	56	82
Production plant and machinery	33	--	33	23	--	23
	68	**75**	**143**	**49**	**56**	**105**

At €17 million, the decrease in leased land and buildings is attributable to the retirement of an office building.

As a rule, leases for realty or personalty include a purchase option. The remaining lease terms vary between 1 and 19 years. Depending on market conditions and contracting date, the interest rates underlying leases range from 5.3 to 8.0 percent. The future lease payments under capital leases, the interest portions included therein, and the present values of future lease payments, which are recognized as financial debts, are tabled below:

Capital leases *€ million*

	2002				**2003**			
	2003 [1]	2004-2007 [1]	after 2008	Total	2004	2005-2008	after 2009	Total
Lease payments	15	38	43	96	12	28	31	71
Discount	(5)	(10)	(10)	(25)	(3)	(8)	(8)	(19)
Present values	**10**	**28**	**33**	**71**	**9**	**20**	**23**	**52**

[1] Prior-year data adjusted

The cash inflow from subleasing tangible assets totaled €7 million in 2003 (up from €4 million). During the noncancelable lease term of the subleased tangible assets, a future cash inflow of an aggregate €16 million (down from €17 million) is expected.

(8)
Financial assets

The major joint ventures' proratable assets, liabilities, income and expenses break down as follows:

Joint ventures *€ million*

		2002	**2003**
Assets [1]	(12/31)	100	35
Equity	(12/31)	6	23
Debt [2]	(12/31)	94	12
Net sales		165	46
EBT		7	9

[1] Including income tax assets, prepaid expenses and deferred charges
[2] Accruals, liabilities, income tax liabilities and deferred income

Except for the other investments, which are carried at cost (an unchanged €1 million), the other long-term securities (€6 million; down from €9 million) have been fair-valued. Liens of €5 million rest on securities to protect employees from insolvency risks, the sale of these securities being hence restricted. All remaining long-term securities are readily available for sale.

The other long-term loans total €3 million (down from €4 million); their book value equals their fair value.

(9)
Inventories

Inventories *€ million*

	12/31/2002	**12/31/2003**
Raw materials and supplies	270	205
Work in process	322	253
Finished products	94	70
Merchandise	62	58
Prepayments made	154	130
	902	**716**
less prepayments received	(40)	(27)
	862	**689**

The book value of inventories stated at the lower NRV totals €184 million (down from €222 million). In the year under review, €2 million (down from €4 million) of inventories previously written down was written up as NRV had risen. Inventories do not collateralize any liabilities.

(10)
Receivables and sundry assets

Receivables and sundry assets *€ million*

	12/31/2002	thereof due after 1 year	**12/31/2003**	thereof due after 1 year
Trade receivables	662	40	490	26
All other receivables and sundry assets				
receivables from l/t manufacturing contracts	226	93	159	9
sundry assets	157	26	141	12
	383	119	300	21
	1,045	**159**	**790**	**47**

Breakdown of receivables from long-term manufacturing contracts:

Receivables from manufacturing contracts *€ million*

	12/31/2002	**12/31/2003**
Production cost incurred	265	177
plus markup (less losses)	63	45
	328	**222**
less prepayments received	(102)	(63)
	226	**159**

Notes (Group)
Notes to the balance sheet

Breakdown of sundry assets:

Sundry assets *€ million*	12/31/2002	**12/31/2003**
Short-term securities	4	2
Other receivables		
non-income taxes	31	31
purchase price balances (sale of realty/shares)	17	13
prepayments made	10	21
financial derivatives	9	17
Miscellaneous current assets	86	57
	157	**141**

The disclosed book values of the monetary assets covered by these items (including securities and receivables from financial derivatives) approximate their fair values.

No accounts were due from nonconsolidated group companies, whether in 2003 or 2002. Accounts due from joint ventures and associated affiliates totaled €13 million (down from €14 million).

Under an ABS program, the Rheinmetall Group sells trade receivables on a revolving basis up to a maximum volume of €127 million. According to IAS 39, sold receivables are treated as disposed of since the residual recourse risks are now insignificant for the Company. As of December 31, 2003, the principal of receivables sold came to €103 million (down from €127 million).

(11)
Cash & cash equivalents

Cash & cash equivalents *€ million*	12/31/2002	**12/31/2003**
Cash on hand and in bank (incl. checks)	367	336

Disposal of cash & cash equivalents is not restricted (down from a €4 million restriction the year before).

(12)
Income tax assets

Income tax assets *€ million*	12/31/2002	**12/31/2003**
Deferred tax assets	65	64
Income tax refundable by the tax office	8	7
	73	**71**

Deferred taxes are allocable to the following balance sheet lines:

Deferred tax assets *€ million*

	12/31/2002		**12/31/2003**	
	Deferred tax assets	Deferred tax liabilities	Deferred tax assets	Deferred tax liabilities
Loss carryovers and tax credits	94	--	73	5
Fixed assets	23	117	25	91
Inventories and receivables	227	202	162	147
Pension accruals	39	--	35	1
Other accruals	34	1	30	--
Liabilities	139	178	142	127
Sundry	15	28	(7)	55
	571	**526**	**460**	**426**
Offset	(506)	(506)	(396)	(396)
	65	**20**	**64**	**30**
thereof not affecting net income		45		44

Apart from the capitalized deferred tax assets from loss carryovers of €73 million (down from €94 million), further tax loss carryovers exist at €404 million (down from €548 million) which were not recognizable, and of which €103 million (down from €258 million) is allocable to loss carryovers for corporate income tax purposes, €18 million (down from €105 million) referring to those for municipal trade tax purposes, another €284 million (down from €294 million) to non-German tax loss carryovers. The German loss carryovers are not subject to expiration whereas the foreign ones as a rule are (e.g., in the United States utilizable within 20 years). Deferred taxes adjusted in prior periods were written up at €13 million (up from €4 million), while deferred tax assets capitalized in previous years were not written down (down from €2 million). According to the German Tax Reduction Act of October 23, 2000, the changeover from the imputation system to the split rate system (split income taxation) is accompanied by a 15-year transition period during which dividends distributed from EK-40 equity portions (formerly subject to the full German corporate income tax) now entail a corporate income tax reduction and those distributed from EK-02 equity portions (exempt from corporate income tax) increase corporate income tax. The potentials for any deferred tax relief and burden amount to €1 million in either case.

(13)
Total equity

Rheinmetall AG's capital stock amounts to an unchanged €92.16 million and is divided into 18 million no-par bearer shares each of fully voting common, and nonvoting preferred, stock. The preferred stock entitles to a preferential, cumulative dividend. Each of the total 36 million no-par shares accounts for €2.56 of the capital stock.

The Executive Board is authorized to raise the capital stock on or before June 24, 2004, after first obtaining the Supervisory Board's approval, by issuing once or several times new stock against cash contributions for an aggregate maximum of €25 million. However, the Executive Board is authorized, subject to the Supervisory Board's prior approval, to exclude the stockholders' statutory subscription rights for up to an aggregate €9.2 million at par in accordance with Art. 186(3)(4) German Stock Corporation Act ("AktG"). Furthermore, the Executive Board may exclude subscription rights for up to an aggregate €1.0 million with respect to stock issued to employees of the Company or subsidiaries controlled by it.

Notes (Group)
Notes to the balance sheet

Röchling Industrieverwaltung GmbH, Mannheim, holds a 42.1-percent stake in Rheinmetall AG's capital stock, viz. 73.7 percent of the voting common, and 10.5 percent of the nonvoting preferred, stock. The additional paid-in capital solely originates from stock premiums from Rheinmetall AG's capital increases.

The other reserves include, besides the reserves retained by Rheinmetall AG from earnings at €288 million (up from €78 million), also the other comprehensive income (OCI), which covers currency translation differences of a negative €41 million (up from an equally negative €30 million), as well as the reserves from fair and other valuation at a total €65 million (virtually unchanged).

The analysis in 2003 of such reserves presents the following picture:

Reserves from fair and other valuation *€ million*

	Land revaluation reserve	Hedge reserve	Securities available for sale	Reserves from fair and other valuation
Jan. 1, 2002	**72**	**(2)**	**(1)**	**69**
Change in fair values	(17)	3	--	(14)
Disposals	(7)	--	--	(7)
Deferred taxes	10	(1)	--	9
Minority interests	8	--	--	8
Dec. 31, 2002	**66**	**--**	**(1)**	**65**
Change in fair values	(4)	7	2	5
Disposals	(10)	--	--	(10)
Deferred taxes	5	(3)	(1)	1
Minority interests	4	--	--	4
Dec. 31, 2003	**61**	**4**	**--**	**65**

Breakdown of the land revaluation reserve:

Breakdown of the land revaluation reserve *€ million*

	12/31/2002	**12/31/2003**
Revaluation of land within tangible assets	116	102
Deferred taxes	(46)	(41)
Minority interests	(4)	--
	66	**61**

The separate financial statements of Rheinmetall AG close the fiscal year with net earnings of €66 million, €24 million thereof being earmarked for distribution of a cash dividend and €42 million for transfer to the reserves retained from earnings. The proposed cash dividends amount to €0.64 and €0.70 per share of common and preferred stock, respectively (up from €0.44 and €0.50, respectively, plus a €0.20 bonus each).

The minority interests mainly refer to the Automotive sector (at €20 million; down from €69 million), and Defence (at €36 million; down from €117 million). In fiscal 2002, the minority interests had included €4 million due to the application of the revaluation method. The prior year minority interests in Electronics came to an additional €21 million.

(14)
Accruals

Accruals *€ million*

	12/31/2002	12/31/2003
Accruals for pensions and similar obligations	660	530
Other accruals	581	489
	1,241	**1,019**

Accruals for pensions and similar obligations

These accruals provide for obligations under vested rights and current pensions payable to eligible active and former employees and their surviving dependants. Such commitments primarily encompass pensions, both basic and supplementary. The individual, confirmed pension entitlements are based on benefits that vary according to country and company and, as a rule, are measured according to service years and employee pay. Moreover, at the German companies, a performance-related pension obligation was incurred whose amount hinges on the achievement of certain benchmarks for the ROCE formula. Being a noncurrent provision for the accumulated postretirement benefit obligation, the accrued health care obligations to the retirees of some US Group companies are also included in the pension accruals recognized hereunder.

The company pension system consists of both defined-contribution and defined-benefit plans. Under a DCP, the company incurs no obligation other than the payment of contributions to earmarked pension funds. These pension expenses are shown within personnel expenses and do not require any provision. In the year under review, a total €78 million (down from €89 million) was paid to DCPs, specifically the Statutory Social Security Insurance in Germany. Among those DCPs where material sums are involved, the earmarked pension funds of the Swiss Group companies, whose employees pay in supplementary contributions, were overfunded as of both December 31, 2003 and 2002. According to the provisions of the underlying bylaws, such excess funds accrue primarily to the beneficiaries and eligible retirees and may not be repaid or refunded, even pro rata, to the Group companies.

Under defined benefit plans, a company is obligated to meet its confirmed commitments to active and former employees.

The following actuarial parameters have been assumed to determine the present value of the DBO:

Pension accruals – parameters %

	12/31/2002		12/31/2003	
	Germany	USA	Germany	USA
Discount rate	5.50	6.50	5.50	6.00
Pay trend (general)	+3.00	+4.00	+3.00	+4.00
Pay trend (fixed-sum commitments)	+1.25	--	+1.25	--
Pension trend	+1.25	--	+1.25	--
Expected return on plan assets	--	9.00	--	9.00

Due to the lower US capital market interest rate level, the discount rate for US pension obligations was reduced by 0.50 percentage points. The non-German pension liabilities primarily refer to benefit obligations incurred by US subsidiaries, certain of which are funded by earmarked funds.

Notes (Group)
Notes to the balance sheet

The pension accruals are derived from the present value of the DBO, as well as from the plan assets:

Pension accruals *€ million*

	2002			**2003**		
	Germany	Abroad	Total	Germany	Abroad	Total
Development of the present value of the DBO						
Present value of the DBO at Jan. 1	611	196	807	619	157	776
Consolidation group changes	(14)	--	(14)	(131)	--	(131)
Reclassified	2	(2)	--	--	--	--
Exchange differences	--	(27)	(27)	--	(23)	(23)
Service cost	15	3	18	13	2	15
Interest cost	34	11	45	32	8	40
Pension payments	(30)	(15)	(45)	(30)	(15)	(45)
Plan curtailments/settlements	--	9	9	--	(1)	(1)
Past service revenue	--	(25)	(25)	--	(1)	(1)
Actuarial (gains)/losses	1	7	8	3	1	4
Present value of the DBO at Dec. 31	**619**	**157**	**776**	**506**	**128**	**634**
Development of plan assets						
Fair value of plan assets at Jan. 1	--	81	81	--	54	54
Exchange differences	--	(11)	(11)	--	(9)	(9)
Expected return on plan assets	--	6	6	--	4	4
Contributions paid to pension plans	--	11	11	--	17	17
Pensions paid by plans	--	(13)	(13)	--	(14)	(14)
Actuarial gains/(losses)	--	(20)	(20)	--	6	6
Fair value of plan assets	**--**	**54**	**54**	**--**	**58**	**58**
Unfunded pension obligations at Dec. 31	**619**	**103**	**722**	**506**	**70**	**576**
Unrecognized actuarial gains/(losses)	(23)	(43)	(66)	(21)	(28)	(49)
Unrecognized past service revenue	--	4	4	--	3	3
Pension accrual as of Dec. 31	**596**	**64**	**660**	**485**	**45**	**530**

As of December 31, 2003, the present value of funded pension obligations amounted to €114 million (down from €129 million). The unrecognized actuarial losses of €49 million (down from €66 million) are attributable to interest rate adjustments, as well as to the variance of the actual from the expected return on plan assets. In the year under review, plan assets actually returned €11 million (up from a prior-year loss of €12 million) before the currency translation losses recognized in equity only and thus clearly outshined expectations. Actuarial losses are released to expense over the average residual service years of the workforce if outside a corridor of 10 percent of total DBO.

Breakdown
of pension expense:

Pension expense *€ million*

	2002			**2003**		
	Germany	Abroad	Total	Germany	Abroad	Total
Service cost	15	3	18	13	2	15
Amortized actuarial gains and losses	--	4	4	--	3	3
Past service revenue	--	(21)	(21)	--	(1)	(1)
Effects of plan settlements/curtailments	--	9	9	--	(1)	(1)
Compounding of expected pension obligations	34	11	45	32	8	40
Expected return on plan assets	--	(6)	(6)	--	(4)	(4)
Total	**49**	**0**	**49**	**45**	**7**	**52**

Except for the interest portion of the annual provision and the expected return on plan assets, which are shown within the net interest result, all of the above lines are recognized as personnel expenses.

Analysis of accruals *€ million*

	1/1/2003	Utilized	Added/ newly provided	Com-pounded	Released	Change in consoli-dation group	Currency differ-ences/ sundry	**12/31/2003**
Pension accruals	**660**	**48**	**18**	**36**	**2**	**(126)**	**(8)**	**530**
[Prior year]	*[673]*	*[43]*	*[31]*	*[39]*	*[21]*	*[(14)]*	*[(5)]*	*[660]*
Other accruals								
Warranties	72	16	32	--	7	(22)	--	59
Identifiable losses	67	43	18	--	11	(1)	8	38
Yet unbilled costs	124	93	102	--	11	(23)	1	100
Restructuring	90	39	38	1	7	(6)	(2)	75
Personnel	127	82	101	--	3	(20)	(2)	121
Remaining accruals	101	56	59	--	17	12	(3)	96
	581	**329**	**350**	**1**	**56**	**(60)**	**2**	**489**
	1,241	**377**	**368**	**37**	**58**	**(186)**	**(6)**	**1,019**

The accruals for restructuring programs mainly provide for the short-term realization of the scheduled personnel retrenchment (including termination benefits, preretirement part-time work).

The remaining accruals cover at €15 million legal, consultancy and audit fees (down from €19 million), at €5 million contractual penalties (down from €8 million), at €9 million bonuses, discounts and rebates (up from €8 million), and at €8 million environmental risks (up from €6 million).

Notes (Group)
Notes to the balance sheet

The following cash outflows are expected from each of the other accrual categories:

Cash outflows of accruals *€ million*

	2002			**2003**		
	< 1 year	1–5 years	> 5 years	< 1 year	1–5 years	> 5 years
Warranties	45	26	1	42	16	1
Identifiable losses	55	10	2	25	6	7
Yet unbilled costs	122	2	--	98	2	--
Restructuring	44	40	6	28	43	4
Personnel	92	23	12	91	19	11
Remaining accruals	75	22	4	70	20	6
	433	**123**	**25**	**354**	**106**	**29**

(15)
Liabilities

Liabilities *€ million*

	12/31/2002	thereof due within <1 year	thereof due after 5 years	**12/31/2003**	thereof due within <1 year	thereof due after 5 years
Financial debts						
bonds	348	--	--	348	--	--
due to banks	176	71	30	122	36	30
under leases	137	10	82	90	10	33
other	7	6	--	6	1	3
	668	**87**	**112**	**566**	**47**	**66**
Trade payables	**475**	**475**	**--**	**455**	**455**	**--**
All other liabilities						
prepayments received on orders	198	93	--	175	59	54
payables under l/t manufacturing contracts	323	79	102	190	17	1
sundry liabilities	223	204	--	209	204	--
	744	**376**	**102**	**574**	**280**	**55**
	1,887	**938**	**214**	**1,595**	**782**	**121**

As from January 1, 2003, commissions payable have been included in trade payables while the year before, they were (at €64 million) part of sundry liabilities. The prior-year comparatives have been restated accordingly.

The bond issue floated in 2001 matures on May 31, 2006.

The financial debts under leases comprise accounts due to the banks of, and owed by, consolidated special-purpose leasing firms at €38 million (down from €66 million). The liabilities due to banks do not include any financial notes payable (unchanged).

€52 million of financial debts (down from €55 million) is collateralized by land charges and similar encumbrances, as is another €38 million (down from €66 million) borrowed to finance the realty owned by consolidated special-purpose leasing firms and encumbered with land charges of €12 million (down from €57 million) whose consolidation is mandatory pursuant to IAS 27 in conjunction with SIC 12.

Breakdown of payables under long-term manufacturing and construction contracts:

Payables under l/t manufacturing contracts *€ million*

	12/31/2002	**12/31/2003**
Prepayments received	366	229
less production cost incurred	(36)	(35)
less markups (plus losses)	(7)	(4)
	323	**190**

The sundry liabilities shown under all other liabilities break down as follows:

Sundry liabilities *€ million*

	12/31/2002	**12/31/2003**
Liabilities for social security	32	27
Due to board members and employees	7	25
Non-income taxes	45	50
Monies in transit from debt collection	59	43
Financial derivatives	5	5
Miscellaneous	75	59
	223	**209**

Trade payables include trade notes payable of €9 million (up from €7 million). The liabilities due to joint ventures and associated affiliates total an aggregate €3 million (down from €17 million). Besides the payables for financial derivatives, the carrying amounts of trade payables and of all other liabilities approximate their fair values.

The analysis below reflects the terms, and book and fair values, of financial debts, the fair values being determined on the basis of interest rates current at the balance sheet date for corresponding maturities/redemption structures:

Bonds *€ million*

Interest terms	Rate (%)	Currency	Maturing in	Book value 12/31/2002	Fair value 12/31/2002	Book value **12/31/2003**	Fair value **12/31/2003**
fixed	6.125	€	2006	348	350	348	351

Notes (Group)
Notes to the balance sheet

Due to banks *€ million*

Interest terms value	Weighted rate (%)	Currency	Maturing in	Book value 12/31/2002	Fair value 12/31/2002	**Book value 12/31/2003**	**Fair value 12/31/2003**
fixed	5.4	div.	2003	12	12	--	--
fixed	2.6	€	2004	48	50	16	16
fixed	2.4	Sfr	2004	5	5	4	4
fixed	7.9	US$	2005	42	48	31	36
fixed	6.2	€	2005	4	4	2	3
fixed	1.0	¥	2006	--	--	3	3
fixed	5.1	€	2006/2007	15	17	10	10
fixed	3.0	US$	2008	--	--	4	4
fixed	5.0	€	2008	--	--	1	1
fixed	5.6	€	2009–2011	5	6	5	5
fixed	4.9	€	2013	--	--	3	3
fixed	5.4	€	2020	26	25	24	25
				157	**167**	**103**	**110**
variable		€	2003/2004	19	19	3	3
variable		Dkr	2006/2007	--	--	16	16
				19	**19**	**19**	**19**
				176	**186**	**122**	**129**

Under leases *€ million*

Interest terms value	Weighted rate (%)	Currency	Maturing in	Book value 12/31/2002	Fair value 12/31/2002	**Book value 12/31/2003**	**Fair value 12/31/2003**
fixed	5.9	€	2003–2006	19	20	12	13
fixed	5.3	€	2008/2009	42	44	31	33
fixed	6.6	€	2010–2012	18	19	9	10
fixed	5.8	€	2015	7	7	6	7
fixed	6.2	Sfr	2015	11	12	9	11
fixed	8.0	€	2020	11	13	11	13
fixed	6.4	€	2021/2022	29	30	12	13
				137	**145**	**90**	**100**

Other *€ million*

Interest terms value	Weighted rate (%)	Currency	Maturing in	Book value 12/31/2002	Fair value 12/31/2002	**Book value 12/31/2003**	**Fair value 12/31/2003**
fixed	5.0	€	2006	5	5	1	1
fixed	7.5	€	2009	--	--	3	3
variable		€	sdry. ≤ 2013	2	2	2	2
				7	**7**	**6**	**6**

(16)
Income tax liabilities

Income tax liabilities *€ million*	12/31/2002	**12/31/2003**
Deferred taxes	20	30
Current income tax liabilities	39	50
	59	**80**

For details and breakdown of deferred tax liabilities, see Note (12).

(17)
Deferred income

Deferred income *€ million*	12/31/2002	**12/31/2003**
Deferred gains from sale-leaseback transactions	6	5
Deferred grants	12	7
Other	13	5
	31	**17**

Notes (Group)
Notes to the consolidated income statement

(18)
Net sales

Net sales *€ million*	2002	**2003**
Net sales (excl. PoC)	4,378	4,142
Revenues according to PoC	193	106
	4,571	**4,248**

(19)
Net inventory changes, other work and material capitalized

Net inventory changes, other work and material capitalized *€ million*	2002	**2003**
Change in inventories of finished products and work in process	(99)	(3)
Other work and material capitalized	35	29
	(64)	**26**

(20)
Other operating income

Other operating income *€ million*	2002	**2003**
Gains from fixed-asset disposal	347	74
Income from the release of badwill	2	1
Income from the release of accruals	61	56
Income from the reversal of bad-debt allowances	14	11
Income from compensation and refunds	7	14
Sundry rental income	9	12
Income from grants and subsidies	7	7
Income from canteens and ancillary operations	3	3
Income from credit notes for prior years	8	7
Income from prototype and tooling costs refunded	9	6
Other secondary income	50	58
	517	**249**

€47 million of the gains from fixed-asset disposal originated from the divestment of Preh-Werke GmbH & Co. KG, Hirschmann Austria GmbH and the operations of STN Atlas Marine Electronics GmbH (down from €314 million).

(21)
Cost of materials

Cost of materials *€ million*	2002	**2003**
Cost of raw materials, supplies, and merchandise purchased	1,838	1,760
Cost of services purchased	239	254
	2,077	**2,014**

(22)
Personnel expenses

Personnel expenses *€ million*	2002	**2003**
Wages and salaries	1,196	1,098
Social security taxes and related employee benefits	153	146
Pension expense	98	95
	1,447	**1,339**

Pension expense also reflects the employer contributions to DCPs (Social Security Insurance in Germany and comparable foreign institutions).

Annual average headcount	2002	**2003**
Automotive	11,685	11,545
Defence	9,056	8,418
Electronics	5,037	3,452
Jagenberg / EMG (financial investees)	1,391	1,621
Others/holding company	568	164
	27,737	**25,200**

(23)
Amortization/depreciation/write-down

For a breakdown by amortization and depreciation, see the fixed-asset analysis.

Write-down was charged to tangible and intangible assets at €17 million (down from €53 million).

Notes (Group)

Notes to the consolidated income statement

(24)
Other operating expenses

Other operating expenses € million	2002	2003
Losses on fixed-asset disposal	13	34
Exit plans, termination benefits, preretirement part-time work	39	42
Selling expenses, commissions	129	105
Maintenance and repair (M&R)	88	92
Promotion and advertising	22	19
Other general administration	165	168
Rents (incl. incidentals)	54	59
Payroll incidentals	35	30
Facility cleaning, security/vigilance	13	12
Outsourced services	10	11
Legal, consultancy and audit fees	51	43
Write-down of receivables	11	12
Non-income taxes	11	13
Additional provisions	109	58
All other	47	24
	797	**722**

(25)
Net interest expense

Net interest expense € million	2002	2003
Interest income		
expected return on plan assets	6	4
other interest and similar income	12	11
	18	**15**
Interest expense		
from capital leases	(6)	(7)
compounding of pension obligations	(45)	(40)
compounding of noncurrent other accruals	(2)	(1)
other interest and similar expenses	(67)	(51)
	(120)	**(99)**
	(102)	**(84)**

(26)
Net investment income and other financial results

Net investment income and other financial results € million	2002	2003
Net investment income		
from joint ventures and associated affiliates	8	9
	8	**9**
Other financial results	(10)	(11)
	(2)	**(2)**

The other financial results comprise a net loss from currency translation of €6 million (up from a net loss of €5 million) and a net gain from financial derivatives of €1 million (down from €3 million). Furthermore, income and expenses generated in connection with securities are, in particular, mirrored in the other financial results.

(27) Income taxes

Income taxes *€ million*

	2002	2003
Current income tax expense	41	51
Deferred taxes	(25)	1
	16	**52**

The table below reconciles the expected to the recognized tax expense. The expected tax expense is determined by multiplying EBT by an unchanged tax rate of 40 percent. This rate covers German corporate income tax, the solidarity surtax thereon, and municipal trade tax. The expected tax is then matched against the effective expense.

Reconciliation of expected to recognized income tax expense *€ million*

	2002	2003
EBT	290	120
Expected income tax expense (tax rate of 40%)	**116**	**48**
Differences from foreign tax rates	(5)	(7)
Losses of subsidiaries not subjected to deferred taxation	11	13
Write-up of deferred tax assets	(4)	(13)
Tax-exempt income and nondeductible expenses	(124)	(10)
Nondeductible goodwill amortization	13	13
Other	9	8
Effective tax expense	**16**	**52**
Effective tax rate in %	**6**	**43**

(28) Minority interests

Minority interests in profit came to €5 million (down from €32 million). The prior-year minority interests included a €4 million share in loss.

Notes (Group)
Notes to the consolidated income statement

(29)
Earnings per share (EpS)

EpS is obtained by dividing the weighted average number of shares issued and outstanding in the fiscal year into the Group's earnings. Neither as of December 31, 2003 nor 2002, were any shares, options or equivalent outstanding that could dilute earnings per share. Therefore, both in the year under review and the previous year, undiluted EpS equals diluted EpS. EpS is determined separately for common and preferred stock with due regard to the latter class's preferential rights to dividends. EpS is, moreover, shown before and after goodwill amortization, "before goodwill amortization" meaning that EpS is disclosed prior to the deduction of €31 million for goodwill amortization (down from €41 million) and after eliminating the income from the release of badwill from capital consolidation of €1 million (down from €2 million).

Earnings per share (EpS) *€ million*

	2002	**2003**
Group earnings (after minority interests)	246	63
Excess dividend (preferred over common = €0.06 per share)	(1)	(1)
Group earnings after minority interests and elimination of excess dividend	245	62
Number of common shares	18 million	18 million
Number of preferred shares	18 million	18 million
Earnings per common share (after goodwill amortization)	€6.81	€1.72
Earnings per preferred share (after goodwill amortization)	€6.87	€1.78
Group earnings (after minority interests) adjusted for excess dividend, goodwill amortization and income from the release of badwill from capital consolidation	284	92
Earnings per common share (before goodwill amortization)	€7.89	€2.56
Earnings per preferred share (before goodwill amortization)	€7.95	€2.62

(30)
Adjusted EBIT

EBIT after adjustment for nonrecurring expenses, losses, income and gains connected with equity interests, realty and restructuring programs breaks down as follows:

Adjusted EBIT *€ million*

	2002	**2003**
Accounting EBIT	**392**	**204**
Nonrecurring expenses, losses, income, gains related to		
shareholdings	(219)	(26)
realty	5	(7)
restructuring	35	52
Adjusted EBIT	**213**	**223**

Note to the cash flow statement

(31)
Cash flow statement

The cash flow statement conforms with IAS 7 and breaks down into the cash flows generated by operating, investing and financing activities. The effects of changes in the consolidation group are eliminated, parity changes, if impacting on cash & cash equivalents, being shown in a separate line. The net cash provided by operating activities included a cash inflow from interest of €11 million (up from €10 million) and a cash outflow for interest of €54 million (down from €60 million). Income taxes paid came to €51 million (up from €46 million), those refunded totaling €11 million (down from €16 million). The dividends received from associated affiliates and investees amounted to €2 million (down from €8 million).

The cash outflow for acquiring consolidated subsidiaries totaled €144 million (down from €174 million) and substantially concerned the purchase of further shares in Kolbenschmidt Pierburg AG and Oerlikon Contraves AG. The disposal of consolidated subsidiaries produced a cash inflow of €114 million (down from €425 million). The acquisitions and disposals were settled entirely in cash. For purchase price details, see the explanations in Note (2) to the consolidation group.

Cash & cash equivalents of €28 million were taken over in the M&A transactions (up from nil) while €53 million (up from €28 million) in cash & cash equivalents was disposed of in divestments.

The decrease in financial debts from €668 million as of December 31, 2002, to €566 million as of year-end 2003 refers at €10 million to noncash transactions (down from €38 million).

Cash & cash equivalents are identical in the cash flow statement and balance sheet.

Notes (Group)
Note to the segment reports

(32)
Segment reports

In accordance with the Rheinmetall Group's internal controlling organization, the Group breaks down into three corporate sectors (primary segments), viz.
- Automotive
- Defence and
- Electronics

as primary segments.

The Others/consolidation column includes, apart from the Group's parent (Rheinmetall AG), Jagenberg and EMG as financial investees, as well as intragroup service and other nonsegment companies, plus consolidation transactions.

For the first time, the Rheinmetall Group publishes two segment report formats. In the segment report according to IFRS, directly allocable transactions and group level valuations have been assigned to the appropriate segment.

Contrary to this reporting format, the Rheinmetall Group is managed and controlled according to different indicators and, therefore, while the accounting policies and methods applied to the IFRS-based consolidated financial statements have been retained, has published a second report in a format that reflects its management and controlling structure. In this format, goodwill amortization and effects of the revaluation of essential land (neither of which are included in the financial statements of the subgroups or segments) are indicated in the Others/consolidation column.

The intersegment transfers are principally priced as if at arm's length.

IFRS segment report

Starting from fiscal 2003, the sales generated by non-German Defence companies are reported according to country of destination; the prior-year data has been restated accordingly.

Self-explanatory, segment EBIT means the segment's earnings before interest and income taxes.

Segment assets and liabilities include the essential assets (excluding cash & cash equivalents and income tax assets) and liabilities (excluding financial debts and income tax liabilities).

The segment expenditures refer to tangible and intangible assets (incl. goodwill) and, therefore, depreciation and amortization also cover goodwill.

Segment report by management structure

The balance sheet lines are reported in line with the Rheinmetall Group's shareholder value concept.

Net financial debts reflect financial debts less cash & cash equivalents. Capital employed (CE) is determined as the aggregate sum of total equity, pension accruals and net financial debts and thus mirrors the net capital employed to generate EBIT. The return on capital employed (ROCE) equals EBIT (according to management structure) divided by average capital employed (average of the balances at December 31, 2002 and 2003).

EBITDA means earnings before interest, taxes, depreciation and amortization. Income from the release of badwill from capital consolidation is hence included in EBITDA. The EBIT margin equals EBIT (according to management structure) divided by total segment sales.

Capital expenditures refer to tangible and intangible assets.

Supplementary disclosures

(33)
Discontinued operations

The financial investee Jagenberg, the Heidel Group parented by Eurometaal Holding Deutschland GmbH and held by Defence, the remaining Electronics operations (Hirschmann and Preh), as well as the companies of financial investee EMG no longer belong in the Rheinmetall Group's core business.

The divestment resolutions were adopted by the Executive Board as follows:
- Financial investee Jagenberg: September 2000
- Heidel Group: November 2001
- Hirschmann Group: June 2003/February 2004
- Preh Group: September 2003
- Financial investee EMG: October 2003

Financial investee Jagenberg, Heidel, Preh, Hirschmann and most of the EMG Group (STN ATLAS Marine Electronics GmbH) were disposed of in fiscal 2003 or Q1/2004 (Heidel/Hirschmann, Neckartenzlingen).

Financial investees Jagenberg and the EMG Group are included in the Others/consolidation segment. The consolidated balance sheet, income statement and statement of cash flows include the discontinued operations at the following amounts:

Balance sheet data *€ million*

	Jagenberg		Heidel		Hirschmann/Preh		EMG		**Total**	
Balance sheet data at Dec. 31	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**
Fixed assets	45	--	9	9	145	53	--	7	199	69
Current assets (excl. cash & cash equivalents)	104	--	37	36	164	91	--	52	305	179
Cash & cash equivalents	7	--	1	2	8	20	--	31	16	53
Income tax assets, prepaid expenses & deferred charges	1	--	1	--	25	13	--	2	27	15
Pension accruals	40	--	--	--	58	37	--	1	98	38
Other accruals	53	--	2	6	58	23	--	1	113	30
Financial debts	17	--	19	15	23	4	--	42	59	61
Trade payables and all other liabilities	25	--	11	10	60	89	--	12	96	111
Income tax liabilities and deferred income	8	--	1	1	23	14	--	8	32	23

Summary of major income and cash flow statement data of discontinued operations (2002 comparatives adjusted):

Income and cash flow data *€ million*

	Jagenberg		Heidel		Hirschmann/Preh		EMG		**Total**	
	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**
Net sales	212	64	69	101	563	501	--	216	844	882
Operating result	(16)	(32)	2	2	(24)	42	--	72	(38)	84
EBT	(21)	(33)	--	1	9	37	--	69	(12)	74
Income taxes	(2)	(10)	--	--	--	4	--	6	(2)	--
Net income/(loss)	**(19)**	**(23)**	**--**	**1**	**9**	**33**	**--**	**63**	**(10)**	**74**
Net gain/(loss) from disposal	(2)	(23)	--	--	--	24	--	21	(2)	22
Net cash (used in)/ provided by operating activities	(6)	(50)	2	7	75	22	--	(2)	71	(23)
Net cash (used in)/ provided by investing activities	30	9	(2)	(3)	(31)	21	--	24	(3)	51
Net cash (used in)/ provided by financing activities	(30)	34	--	(35)	(40)	(42)	--	(14)	(70)	(57)
Change in cash & cash equivalents	**(6)**	**(7)**	**--**	**(31)**	**4**	**1**	**--**	**8**	**(2)**	**(29)**

Notes (Group)
Supplementary disclosures

(34) Contingent liabilities and assets

Contingent liabilities and assets *€ million*

	2002	**2003**
Contingent liabilities		
from notes endorsed and discounted	2	--
under bonds and guaranties (incl. for drafts, notes and checks)	81	48
under warranty and indemnity agreements	152	41
	235	**89**

A joint and several liability exists for the debts assigned under the split-up of Bremen-based STN Atlas Elektronik GmbH, to Atlas Elektronik GmbH, Bremen, at an non-specifiable amount.

In the judicial review proceedings pending since 1998, the share exchange ratio determined during the Kolbenschmidt Pierburg merger (Rheinmetall Beteiligungen) is examined for fair valuation. The expert appointed by the Heilbronn Regional Court has meantime submitted on the basis of provisional figures an interim report that arrives at significantly different values for the companies merged in January 1998. However, after perusing and scrutinizing this interim report, Kolbenschmidt Pierburg AG sees no reason for departing from the originally determined value relations as these were determined by two independent accounting and auditing firms when the merger was transacted and then endorsed by a court-appointed merger expert accountant. Kolbenschmidt Pierburg assumes that the values determined by three independent experts will prevail in a final review and re-examination. No further disclosures are made lest the outcome of the proceedings should be biased.

Moreover, a performance bond exists at €98 million (down from €99 million) in favor of a nonconsolidated Rheinmetall investee; however, in the relationship of the investee's shareholders inter se, Rheinmetall's liability is limited to 9.33 percent.

From a number of lawsuits instituted by Rheinmetall, certain contingent assets exist whose amount can currently not be estimated.

(35) Other financial obligations

As of December 31, 2003, the commitments to purchase tangible and intangible assets for capital expenditure projects totaled €10 million (down from €33 million). In addition, obligations under other agreements and contracts exist at €38 million (up from €24 million).

In the year under review, rents of €55 million (up from €51 million) were expensed as paid under operating leases for the entire computer hardware/software and other assets.

The following cash outflows under such operating leases are expected in future periods:

Cash outflows under operating leases *€ million*

	2003	2004–2007	after 2007	Total	2004	2005–2008	after 2008	Total
Buildings	18	42	64	124	22	66	66	154
Other leases	30	66	23	119	17	32	--	49
	48	108	87	243	39	98	66	203

(36)
Stock appreciation rights (SARs)

For 1998 to 2001, the Rheinmetall Group has granted qualifying managerial staff SARs for them to participate in any stock appreciation. SAR programs are basically phantom stock option plans under which participants receive a cash compensation upon exercise that equals the difference between the stock price at exercise date and the base (reference) price. The base price has been fixed at the arithmetic mean of the closing prices of Rheinmetall preferred and common stock as quoted on the 10 market days preceding plan commencement.

In addition, the Automotive sector launched a similar program that uses the price trend of Kolbenschmidt Pierburg stock as benchmark.

The SAR programs have an overall term of 7 years each: after a 3-year qualifying period, SARs may be exercised during defined time (or opportunity) windows during the residual 4-year term. If not exercised during such period or when eligible staff leave Rheinmetall for any reason other than retirement or death, the SARs become forfeited and lapse. SARs cannot be exercised unless and until the base price has been exceeded by 25 percent or more on the day of exercise.

Key parameters of the SAR programs launched to date:

SAR programs

SAR program	Exercisable after	Base price €	[i] Number issued	[i] thereof forfeited after 12/31/2002	thereof forfeited in 2003	thereof exercised/ paid in settlement in 2003	SARs as of 12/31/2003
Rheinmetall stock							
1998	end-2001	18.09	310,000	50,000	0	220,000	40,000
1999	end-2002	12.95	871,500	196,000	26,000	629,000	20,500
2000	end-2003	9.24	912,000	167,500	52,500	647,500	44,500
2001	end-2004	16.50	864,000	62,000	74,000	703,000	25,000
			2,957,500	475,500	152,500	2,199,500	130,000
Kolbenschmidt Pierburg stock							
1999	end-2002	15.07	250,000	50,000	7,500	192,500	0
2000	end-2003	13.20	245,000	45,000	7,500	192,500	0
2001	end-2004	11.88	222,500	5,000	10,500	207,000	0
			717,500	100,000	25,500	592,000	0

[i] *adjusted*

Obligations under SARs are measured at fair value pro rata temporis by using an option price model and distributed over the qualifying period. An accrual of €1 million (down from €4 million) provides for the obligations incurred up to December 31, 2003.

In November 2003, the Executive Board submitted to the SAR holders a compensation offer for the 2000 and 2001 SAR plans not yet due. The share price underlying the compensation offer was determined as the arithmetic mean of the closing prices quoted at the Frankfurt/Main Stock Exchange (floor trading) during the 10 trading days preceding November 4, 2003.

Under the compensation offer, 1,750,000 options of a total value of €19 million were paid out in settlement.

Notes (Group)
Supplementary disclosures

(37)
Hedging policy and financial derivatives

The operations and financing transactions of Rheinmetall as an international group are exposed to financial risks, mainly from liquidity, counterparty failure, exchange rate volatility and interest rate changes. In accordance with the groupwide implemented risk management system of Rheinmetall AG, such risks are not only identified, analyzed and measured but also managed through derivative financial instruments. No such derivatives may be acquired for speculation. All transactions involving financial derivatives are subject to stringent monitoring, which is particularly ensured through the strict segregation of the contracting, settlement and control functions.

Liquidity risk

Sufficient liquidity at all times is ensured by the Rheinmetall Group especially by a cash budget and forecast over a specified period, as well as through existing, unutilized credit facilities.

Counterparty risk

The Rheinmetall Group supplies mostly customers of prime standing, which downscales the risk of counterparty failure or default to an extremely low level. According to current facts, the collection risk is covered by bad-debt and equivalent allowances. Over and above this scope, the Rheinmetall Group has not extended any major credits to specific parties.

The default risk from financial derivatives is the potential failure of a counterparty and is therefore capped by the positive fair value due from any such counterparty. Counterparties of Rheinmetall Group companies for contracting financial derivatives are exclusively German and foreign banks of prime standing. By setting these high standards on counterparties, the risk of uncollectible debts is minimized.

Currency risk

Due to the international nature of the Rheinmetall Group's business, certain operational currency risks arise from the fluctuating parity of the transaction currency to other currencies. Open positions exposed to a currency risk are principally hedged through financial derivatives, generally currency forwards or futures but also currency options and swaps. These hedges are contracted at corporate sector level.

Interest rate risk

For the Rheinmetall Group's financing activities, such funding tools as floating-rate facilities are used, too. Interest rate hedges like caps/floors/collars and interest rate swaps contain the risks emanating from market rate changes. These hedges are contracted centrally by Rheinmetall AG, as well as locally at subsidiary or subgroup level.

As of December 31, 2003, the currency and interest rate hedges tabled below have existed, their notional volumes being shown non-netted and thus reflecting the total amounts of all individual contracts. Being marked to the market at December 31, the fair values of financial derivatives correspond to prices in arm's length transactions.

Hedges *€ million*

	Notional volume		Maturing after 1 year		Fair market values	
	12/31/2002	**12/31/2003**	12/31/2002	**12/31/2003**	12/31/2002	**12/31/2003**
Currency hedges						
Currency forwards/futures	287	245	51	31	6	13
Other	4	31	--	--	--	1
	291	**276**	**51**	**31**	**6**	**14**
Interest rate hedges						
Options	125	125	95	--	--	--
Swaps	32	24	31	24	(3)	(2)
	157	**149**	**126**	**24**	**(3)**	**(2)**
Other hedges						
Other hedges	10	--	5	--	1	--

Although the derivative transactions contracted within the Rheinmetall Group as part of the corporate risk management policy represent hedges at the economic level, they fail virtually throughout to satisfy the IFRS hedge recognition criteria. Consequently, the volume of cash flow hedges is immaterial.

(38)
Other details of transactions with related parties

The subsidiaries consolidated by Rheinmetall AG directly or indirectly maintain ordinary business relations with a few nonconsolidated Group companies, as well as associated affiliates and joint ventures. Any and all trade transactions conducted in the scope of ordinary day-to-day business with unconsolidated related companies conform with the arm's length principle.

Volume of major services provided to/by related companies:

Services provided to/by related companies *€ million*

	Volume of services rendered		Volume of services utilized	
	2002	**2003**	2002	**2003**
GIWS Gesellschaft für intelligente Wirksysteme GmbH	32	18	--	--
Microlog Logistische Dienstleistungen GmbH	1	--	10	5
PSM Project, System & Management GmbH	--	11	--	--
Pierburg Instruments GmbH	1	1	--	--
Kolbenschmidt Shanghai Piston Co. Ltd.	--	--	2	2
	34	**30**	**12**	**7**

All of the aforesaid companies are carried at equity.

There were no reportable transactions with individuals related to the Rheinmetall Group.

Notes (Group)
Supplementary disclosures

(39)
Supervisory and Executive Boards

Supervisory Board
Supervisory Board fees amounted to an unchanged €0.9 million in fiscal 2003. Neither was any further compensation paid, nor were any benefits granted, to Supervisory Board members for personally rendered advisory or agency services in the year under review.

Executive Board
For their duties performed on behalf of the parent and its subsidiaries, Executive Board members received a total €12.5 million in the year under review (up from €3.9 million), breaking down into €1.7 million of fixed remuneration (up from €1.5 million) and €3.0 million of profit shares (up from €2.3 million), plus compensation in kind at €0.1 million (unchanged). The latter was substantially paid in the form of company car use and grants for social security insurance. In addition, the Executive Board members received compensation of €2.9 million for phantom stock under the SAR programs which were launched in 1998 and granted for the last time in 2001. These payments have been made in compensation for all SARs previously granted to Executive Board members. For further details of the SAR programs, see Note (36) above. Moreover, a new incentive program supersedes and replaces the terminated SAR plans that is based on the absolute increase in the Rheinmetall Group's shareholder value; €4.8 million was paid in 2003 under this incentive program.

A total €2.2 million was paid to former Executive Board members and their surviving dependants (up from €1.7 million). Pension obligations to former Management or Executive Board members and their surviving dependants exist at a total €12.6 million (down from €17.8 million).

Shareholdings
As of December 31, 2003, none of Rheinmetall AG's Supervisory or Executive Board members held any reportable shares in the Company.

(40)
Corporate Governance Code

In December 2003/February 2004, Rheinmetall AG published on the Internet at www.rheinmetall.com/cg.php, and thus made available to its stockholders, the declaration of conformity according to the German Corporate Governance Code pursuant to Art. 161 AktG. Regarding the listed subsidiary included in the consolidated financial statements of Rheinmetall AG, Kolbenschmidt Pierburg AG, the declaration of conformity under the terms of Art. 161 AktG has been published since December 2003 on the Internet at www.kolbenschmidt-pierburg.com.

Düsseldorf, March 10, 2004

Rheinmetall AG
The Executive Board

Eberhardt Dr. Kleinert Dr. Müller

Major Group companies

Fully consolidated companies

	Interest held %	Equity as of 12/31/2003 [1] € million	Net sales 2003 [1] € million
Rheinmetall AG, Düsseldorf	**--**	**447.9**	**0.0**
Kolbenschmidt Pierburg AG, Düsseldorf	**95.53**	**286.5**	**0.0**
KS Kolbenschmidt GmbH, Neckarsulm	95.53	176.0	225.6
Société Mosellane de Pistons S.A., Basse-Ham (Thionville), France	95.53	20.2	43.0
Karl Schmidt Unisia Inc., Marinette, USA	87.89	4.3	220.8
KS Pistões Ltda., Nova Odessa, Brazil	95.53	36.1	91.3
KS Gleitlager GmbH, St. Leon-Rot	95.53	13.7	135.2
MSI Motor Service International GmbH, Neckarsulm	95.53	15.5	104.9
KS Aluminium-Technologie AG, Neckarsulm	95.53	20.4	159.7
Pierburg GmbH, Neuss	95.53	112.2	491.5
Carbureibar S.A., Abadiano, Spain	95.53	36.3	147.0
Pierburg S.à r.l., Basse-Ham (Thionville), France	95.53	28.8	119.5
Pierburg S.p.A., Lanciano, Italy	95.53	15.4	116.5
Rheinmetall DeTec AG, Ratingen	**100.00**	**222.8**	**42.4**
Rheinmetall Defence Electronics GmbH, Bremen	100.00	47.8	399.6
Rheinmetall Landsysteme GmbH, Kiel	100.00	19.7	319.5
Nitrochemie Aschau GmbH, Aschau	55.00	24.6	68.4
Nitrochemie Wimmis AG, Wimmis, Switzerland	55.00	33.6	28.2
Mauser-Werke Oberndorf Waffensysteme GmbH, Oberndorf	100.00	13.4	52.8
Rheinmetall W&M GmbH, Unterlüss	100.00	49.7	208.9
Oerlikon Contraves AG, Zurich, Switzerland	100.00	87.2	200.1
Oerlikon Contraves Pyrotech AG, Zurich, Switzerland	100.00	22.1	47.8
Oerlikon Contraves Inc., St. Jean-sur-Richelieu, Canada	100.00	19.6	49.9
Oerlikon Contraves S.p.A., Rome, Italy	100.00	31.1	57.0
Others			
Hirschmann Electronics GmbH & Co.KG, Neckartenzlingen	100.00	72.7	230.0
EuroCom Industries A/S, Ålborg, Denmark	88.59	6.4	47.6

[1] *according to IFRS*

Companies stated at equity

	Interest held %	Equity as of 12/31/2003 [1] € million
Joint ventures		
Kolbenschmidt Pierburg Shanghai Nonferrous Components Co.Ltd. Shanghai, China	47.77	22.6
Kolbenschmidt Shanghai Piston Co. Ltd., Shanghai, China	47.77	23.6
Associated affiliates		
Pierburg Instruments GmbH, Neuss	46.81	17.5

[1] *according to IFRS*

Auditor's report and opinion

Rheinmetall AG, Düsseldorf

Independent group auditor's report and opinion

We have audited the consolidated financial statements prepared by Rheinmetall AG and consisting of balance sheet, income statement, statement of changes in equity, cash flow statement and the notes thereto, for the fiscal year ended December 31, 2003. The consolidated financial statements in accordance with the International Financial Reporting Standards (IFRS) are the responsibility and assertions of the Company's Executive Board. Our responsibility is, based on our audit, to express an opinion on whether the consolidated financial statements conform with IFRS.

We have conducted our audit of the consolidated financial statements in accordance with German auditing regulations and with due regard to generally accepted standards on the audit of financial statements as established by IDW, the Institute of Sworn Public Auditors & Accountants in Germany. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of any material misstatement. When planning the audit procedures, knowledge and understanding of the group's business, its economic and legal environment as well as sources of potential errors are given due consideration. An audit includes examining, on a test basis, the evidence supporting the amounts and disclosures in the consolidated financial statements. The audit also involves assessing the accounting principles used, and significant estimates made, by the Executive Board, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

Based on our audit, it is our opinion that the consolidated financial statements, in accordance with IFRS, present a true and fair view of the group's net assets, financial position and results of operations as well as of its cash flows in the fiscal year under review.

Our audit, which in accordance with German auditing regulations also covered the group management report as prepared by the Executive Board for the fiscal year ended December 31, 2003, has not resulted in any objections or exceptions. It is our opinion that the group management report presents fairly both the group's overall position and the risks inherent in its future development.

In addition, we confirm that the consolidated financial statements and group management report for the fiscal year ended December 31, 2003, satisfy the requirements for exempting the Company from preparing consolidated financial statements and a group management report in accordance with German law.

Düsseldorf, March 11, 2004

PwC Deutsche Revision
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

(Pape)	(Bovensiepen)
Wirtschaftsprüfer	Wirtschaftsprüfer

Balance sheet of Rheinmetall AG as of December 31, 2003 (according to HGB)

ASSETS € '000	12/31/2002	12/31/2003
Fixed assets		
Intangible assets	0	1
Tangible assets	34,047	32,325
Financial assets	423,210	490,476
	457,257	**522,802**
Current assets		
Receivables and sundry assets		
Due from Group companies	520,015	330,432
Sundry assets	15,164	18,353
Cash on hand in bank	235,923	172,963
	771,102	**521,748**
Prepaid expenses & deferred charges	**1,117**	**789**
	1,229,476	**1,045,339**

EQUITY & LIABILITIES € '000	12/31/2002	12/31/2003
Capital stock	92,160	92,160
Additional paid-in capital	208,262	208,262
Reserves retained from earnings	79	46,080
Net earnings	24,120	65,666
Stockholders' equity	**324,621**	**412,168**
Untaxed/special reserves	**3,653**	**3,560**
Accruals		
Accruals for pensions and similar obligations	17,184	20,952
All other accruals	21,476	46,524
	38,660	**67,476**
Liabilities		
Bonds	350,000	350,000
Trade payables	234	622
Due to Group companies	498,568	173,716
Sundry liabilities	13,740	37,797
	862,542	**562,135**
	1,229,476	**1,045,339**

Income statement of Rheinmetall AG for the year ended December 31, 2003 (according to HGB)

€ '000	2002	2003
Income from investments	(7,018)	142,815
Net interest expense	(19,039)	(14,554)
Net financial result	**(26,057)**	**128,261**
Other operating income	72,447	51,554
Personnel expenses	(12,633)	(27,322)
Amortization/depreciation/write-down	(1,800)	(1,706)
Other operating expenses	(24,054)	(31,205)
Earnings before taxes (EBT)	**7,903**	**119,582**
Income taxes	(2,400)	(7,915)
Net income	**5,503**	**111,667**
Transfer from reserves retained from earnings	18,617	--
Transfer to reserves retained from earnings	--	(46,001)
Net earnings	**24,120**	**65,666**

The separate financial statements of Rheinmetall AG, which were prepared in accordance with German Commercial Code (HGB) regulations and on which PwC Deutsche Revision Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Düsseldorf, issued its unqualified auditor's opinion, may be ordered as hard copy (in German language only) from the Company, phone (+49-211) 473-4718, fax (+49-211) 473-4157.

Supervisory Board of Rheinmetall AG

Supervisory Board

Klaus Greinert
Mannheim

Chairman

Chairman of the Röchling Family Council

DeTeWe–Deutsche Telephonwerke AG & Co. KG
DURAVIT AG
(chairman)
DURAVIT S.A.
Rheinmetall DeTec AG
(as from 3/1/2004, chairman as from 3/16/2004)
Advisory board of Gebr. Röchling KG
(chairman)
Advisory board of Röchling Immobilien GmbH
Shareholder committee of Röchling Industrie Verwaltung GmbH

Joachim Stöber *
Biebergemünd

Vice-Chairman

Secretary to the Metalworkers Union's General Secretariat

Blaupunkt GmbH (up to May 2003)
GEA AG
(vice-chairman)
Pierburg GmbH (as from 3/26/2003)

Dr. Eckhard Cordes
Stuttgart

Executive board member of DaimlerChrysler AG

Detroit Diesel Corporation
(chairman)
European Aeronautic Defence and Space Company EADS N.V.
EvoBus GmbH
(chairman)
Deutsche Messe AG
Deutsche BP AG
MTU Motoren- und Turbinen-Union Friedrichshafen GmbH
(chairman)

Dr. Ludwig Dammer *
Düsseldorf

Head of Strategic Production Planning,
Pierburg GmbH

Kolbenschmidt Pierburg AG

Egon Friedel *
Bad Neustadt/Saale
(up to 10/31/2003)

Works council chairman of Preh-Werke GmbH & Co. KG

Dr. Andreas Georgi
Glashütten

Executive board member of Dresdner Bank AG

Allianz Dresdner Asset Management Deutschland GmbH
Allianz Dresdner Bauspar AG
(chairman)
Asea Brown Boveri AG
Deutsche Schiffsbank AG
(chairman)
Deutscher Investment-Trust
Gesellschaft für Wertpapieranlagen mbH
Dresdner Bank Luxembourg S.A.
(vice-president)
Dresdner Bank (Schweiz) AG
(president)
Eurohypo AG
Felix Schoeller Holding GmbH & Co. KG
Oldenburgische Landesbank AG
(chairman)
Reuschel & Co.
(vice-chairman)
RWE Dea AG
Stinnes AG (up to 11/27/2003)

Dr. Horst Girke
Germering
(up to 12/31/2003)

Dipl.-Ing.

DeTeWe - Deutsche Telephonwerke AG & Co. KG

Hans-Peter Haug *
Schlaitdorf
(as from 11/7/2003)

Works council chairman of Hirschmann
Electronics GmbH & Co. KG

Aditron AG (up to 10/15/2003)

* employee representative

Dr. Bernd Michael Hönle
Weisenheim am Sand

Management board member of Röchling Industrie Verwaltung GmbH

Aditron AG (up to 10/15/2003)
BEA Holding AG
DeTeWe-Deutsche Telephonwerke Beteiligungs AG
Francotyp-Postalia Beteiligungs AG
Kolbenschmidt Pierburg AG
PFEIFFER & MAY Großhandel AG
Rheinmetall DeTec AG
Seeber Beteiligungs AG

Reinhard Kiel *
Frankfurt/Main

Secretary to the German Metalworkers Union's General Secretariat

Rheinmetall DeTec AG
(vice-chairman)

Heinrich Kmett *
Fahrenbach/Robern

Works council chairman of KS Kolbenschmidt GmbH

Kolbenschmidt Pierburg AG

Erik Merks *
Hamburg
(up to 10/31/2003)

Works council chairman of SAM Electronics GmbH

SAM Electronics GmbH

Johannes Frhr. v. Salmuth
London, UK

Dipl.-Volkswirt

Supervisory board of Aluminium-Werke Wutöschingen AG & Co.
Röchling Family Council
Advisory Board of Gebr. Röchling KG
Shareholder committee of Röchling Industrie Verwaltung GmbH

Dr. Dieter Schadt
Mülheim/Ruhr
(as from 1/22/2004)

Former CEO of Franz Haniel & Cie GmbH

Delton AG
Esso Deutschland GmbH
ExxonMobil Central Europe Holding GmbH
LSG Lufthansa Service Holding AG
Advisory board of Gebr. Röchling KG
Shareholder committee of Röchling Industrie Verwaltung GmbH
RWE Umwelt AG
TAKKT AG

Wolfgang Tretbar *
Nettetal

Works council chairman of Pierburg GmbH, Nettetal plant

Dr. Sabine Thürmel
Grünwald

Computer scientist

DeTeWe-Deutsche Telephonwerke Beteiligungs AG
Advisory board of Gebr. Röchling KG
Shareholder committee of Röchling Industrie Verwaltung GmbH

Harald Töpfer *
Kassel
(as from 2/9/2004)

Works council chairman of Rheinmetall Landsysteme GmbH, Kassel operation

Gisela Walter *
Ahnatal
(up to 12/31/2003)

Works council chairwoman of Rheinmetall Landsysteme GmbH, Kassel operation

Peter Winter *
Achim
(as from 11/7/2003)

Works council member of Rheinmetall Defence Electronics GmbH

Prof. Dr. Dirk Zumkeller
Munich

Full professor of transport & transit systems, Technical University of Karlsruhe

Kolbenschmidt Pierburg AG
Advisory board of Gebr. Röchling KG
Shareholder committee of Röchling Industrie Verwaltung GmbH
(vice-chairman)

Executive Board members and senior executive officers

Executive Board

Klaus Eberhardt
Düsseldorf

Chairman
Director of Industrial Relations

CEO of Rheinmetall DeTec AG
(as from 3/1/2004)

Membership in supervisory boards

Aditron AG
(chairman, up to 10/15/2003)

Shareholder Committee of EMG EuroMarine Electronics GmbH
(chairman up to 12/1/2003)

Jagenberg AG
(chairman up to 8/27/2003)

Kolbenschmidt Pierburg AG
(chairman)

Shareholder Committee of Preh-Werke GmbH & Co. KG
(chairman up to 10/31/2003)

Rheinmetall Defence Electronics GmbH
(as from 3/1/2004, chairman as from 3/16/2004)

Rheinmetall DeTec AG
(chairman up to 2/29/2004)

STN Atlas Marine Electronics GmbH
(chairman 4/1 to 10/31/2003)

Dr. Gerd Kleinert
Gottmadingen

Automotive

Membership in supervisory boards

Carbureibar S.A.

Shareholder committee of EMG EuroMarine Electronics GmbH
(up to 12/1/2003)

Karl Schmidt Unisia Inc.
(chairman)

KS Aluminium-Technologie AG
(chairman)

KS Gleitlager GmbH
(chairman)

KS Kolbenschmidt GmbH
(chairman)

Pierburg GmbH
(chairman)

Pierburg S.p.A.

STN Atlas Marine Electronics GmbH
(chairman up to 4/1/2003)

Dr. Ernst-Otto Krämer
Meerbusch
(up to 2/29/2004)

Defence

Membership in supervisory boards

GIWS Gesellschaft für intelligente Wirksysteme mbH
(up to 2/29/2004)

Michelin Reifenwerke
(up to 2/29/2004)

Nitrochemie AG
(president up to 2/29/2004)

Nitrochemie Wimmis AG
(chairman up to 2/29/2004)

Oerlikon Contraves
(president up to 2/29/2004)

Rheinmetall Defence Electronics GmbH
(chairman 6/13/2003 to 2/29/2004)

Rheinmetall Landsysteme GmbH
(chairman up to 2/29/2004)

Rheinmetall W&M GmbH
(chairman up to 2/29/2004)

Dr. Herbert Müller
Essen

Finance & Controlling

Membership in supervisory boards

Aditron AG
(up to 10/15/2003)

Kolbenschmidt Pierburg AG

Shareholder committee of Preh-Werke GmbH & Co. KG
(4/29 to 10/31/2003)

Rheinmetall DeTec AG

Senior Executive Officers

Dr. Andreas Beyer
Law, Internal Auditing, M&A

CEO of Jagenberg AG
(up to 8/25/2003)

Membership in supervisory boards

Aditron AG
(up to 10/15/2003)

Jagenberg AG
(as from 9/16/2003)

Kolbenschmidt Pierburg AG
(as from 5/21/2003)

Pierburg GmbH
(as from 10/1/2003)

Heinz Dresia
Controlling and Corporate Development
(1/1 to 9/30/2003)

Management board member of EMG EuroMarine Electronics GmbH
(1/1 to 3/31/2003)

Management board member of DEBEG GmbH
(1/1 to 10/20/2003)

Membership in supervisory boards

EuroCom Industries A/S
(as from 1/1/2003; chairman as from 11/24/2003)

STN Atlas Marine Electronics GmbH
(4/1 to 10/31/2003)

Ingo Hecke
Human Resources and Senior Management

Membership in supervisory boards

Aditron AG
(up to 10/15/2003)

Jagenberg AG
(up to 8/27/2003)

Rheinmetall Defence Electronics GmbH
(up to 3/1/2004)

Financial glossary

Actuarial gains and losses
The actuarial computation of pension accruals is largely based on forecasted parameters (such as pay and pension trends). If these assumptions are changed on the basis of actual developments, actuarial gains or losses result.

Added value
Value added to assets used in production. Internally, Rheinmetall derives added value from income statement data by deducting from the entire annual economic output the year's input, such as cost of materials or amortization/depreciation.

Capital employed (CE)
CE provided by →stakeholders and comprising net financial debts, pension accruals and equity. The meaningful interpretation of this indicator requires→EBIT to calculate →ROCE: EBIT should ensure a sufficient return on CE to satisfy the stakeholders concerned.

Cash flow (gross, but after taxes)
Net income/net loss plus amortization/depreciation and changes in accruals for pensions and similar obligations. This indicator shows a company's ability to internally fund its expenditures and processes and to distribute cash dividends.

Corporate governance
Responsible management and control of a company. The German Corporate Governance Code has compiled certain standards to facilitate comparisons of governance structures between internationally operating German companies. All German listed corporations are required by the law to annually issue a declaration on the extent of past and/or present compliance with the Code's recommendations.

Deferred taxes
Balance sheet line to disclose temporary differences between tax bases and financial accounting values in order to report tax expense in line with pretax accounting income.

EBIT
Earnings before interest and taxes; used to assess a company's performance irrespective of its financing structure. Key indicator for the Rheinmetall Group's management to control group performance.

EBIT margin
Ratio of EBIT to net sales; the percentage is used to compare the profitability of companies of different size. EBIT margins typically vary by type of business.

EBITDA

Earnings before interest, taxes, depreciation and amortization; being a pretax performance indicator that disregards the corporate financing structure and all noncash expenses, EBITDA reflects the gross cash inflow generated by a company.

EBT

Earnings before taxes: the pretax profit/loss after financing expenses is better suited to inform stockholders about the year's performance than net income/loss since tax payments may distort the picture due to past events or special factors.

EpS before/after goodwill amortization

Earnings (net income after ‡goodwill amortization) related to the number of shares issued and outstanding; not identical with the dividend and primarily used to assess a company's results of operations. To compare several companies, the investor calculates the price-earnings ratio (PER) by relating EpS to the stock price. Since goodwill amortization neither reduces cash nor decreases value and, moreover, is not obligatory in all accounting systems, EpS before goodwill amortization is computed alternatively.

Financial derivatives

Financial instruments (e.g., options, futures) derived from original instruments (such as equities, bonds, foreign currency) and used, inter alia, to hedge against currency and interest rate risks. The prices of derivatives hinge directly or indirectly on the value of the underlying transaction.

Free float

Self-explanatory, the freely exchange-tradable shares available to the general public as opposed to stakes owned long term by major investors.

Goodwill

In company acquisitions, net equity under cost (or prorated net assets over cost); requires capitalization as an intangible.

Interest rate swap

Swaps interest payments between two parties, such as variable for fixed rates or vice versa.

International Accounting Standards Board (IASB)

Private-law organization that issues the →International Financial Reporting Standards (IFRS). At its inception in 2001, the IASB adopted the entire set of International Accounting Standards (IAS) published by its predecessor, the IASC.

Financial glossary

International Financial Reporting Interpretations Committee (IFRIC)	Once approved by the →IASB, the IFRIC Interpretations resolve potentially contentious accounting issues and, when declared effective, are binding on all IFRS users.
International Financial Reporting Standards (IFRS)	Standards developed by the IASB primarily to represent financial information for decision-making purposes that is addressed to a broad range of users, mainly investors.
Investment ratio	Ratio of additions to tangible and intangible assets (excl. goodwill) to net sales.
MDAX®	This German midcap index covers 50 (70 prior to 3/24/2003) companies of the Prime Standard from classical sectors. These equities rank directly after the 30 DAX® companies in terms of order book sales and market capitalization, besides dividend payments (performance index).
Net financial debts	All interest-bearing liabilities (such as bonds, accounts due to banks) less cash & cash equivalents. This figure provides information about a company's net indebtedness.
Net leverage	Ratio of →net financial debts to equity: the lower this ratio is the less depends a company on debt.
Percentage of completion	According to IAS 11, method of accounting for long-term construction or service contracts with customers. Net sales, contract costs and contract profits/losses are recognized at their percentage of completion (PoC), although the contract may not have been fully completed and billed to the customer.
Preferred stock	Entitles to a higher dividend than common stock but is (mostly) nonvoting.
Projected unit credit (PUC) method	The PUC method (under IAS 19) is used to provide for pensions and similar obligations. Based on the present value of the DBO, not only the pensions and vested rights (entitlements) as of the balance sheet date are taken into account but also future pay and pension rises.

ROCE (return on capital employed)
Rheinmetall determines this performance indicator as the ratio of →EBIT to the annual average →capital employed. The stakeholders concerned can thus rate the profitability of the capital employed within the company. To add value, ROCE should exceed the percentage cost of capital. If defined identically, ROCE permits a comparison of the profitability of different companies. The ratio is used by management within the Rheinmetall Group for controlling purposes in line with the shareholder value concept.

Segment assets
All assets less cash & cash equivalents and income tax assets.

Segment liabilities
All liabilities less financial debts and income tax liabilities.

Stakeholders
Parties that contribute to corporate performance and put demands on the company in various ways; they mainly include stockholders, banks, lenders, customers, employees, government agencies.

Syndicated loan
Credit facility provided to a company not only by one but several banks (banking syndicate).

Working capital
Net inventories plus trade receivables (including PoC), less prepayments received and trade payables (including PoC) and less accruals for yet unbilled costs. This short definition of (net) working capital within the Rheinmetall Group includes only parameters relevant to corporate governance and control and provides information about the financial resources tied up in WC, which is a material, quickly controllable component of →capital employed. Reducing WC releases financial resources, raises →ROCE and also shareholder value.

Imprint

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Rheinmetall's homepage at **www.rheinmetall.com** contains detailed business information about the Rheinmetall Group and its subsidiaries, present trends, 15-minute stock price updates, press releases, and ad hoc notifications. In fact, investor information is a regular fixture of this website from where all the relevant details may be downloaded.

Our annual report is downloadable from **www.rheinmetall.com** in both English and German, the latter version prevailing in any case of doubt, or may be obtained directly from the Company.

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